

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

**NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

A. Basis of Presentation - The accompanying financial statements of the State of Tennessee have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board. The financial statements of the Colleges and Universities have been prepared in conformity with generally accepted accounting principles for colleges and universities as prescribed by the Governmental Accounting Standards Board. Certain amounts presented for the preceding year have been reclassified for comparative purposes.

B. Financial Reporting Entity

Introduction - As required by generally accepted accounting principles, these financial statements present the primary government and its component units, entities for which the government is considered to be financially accountable. Discretely presented component units are reported in a separate column in the combined financial statements to emphasize they are legally separate from the primary government.

Discretely Presented Component Units.

1. The Tennessee Student Assistance Corporation (TSAC) (Governmental Fund Type) is responsible for guaranteeing student loans under both federal and state programs and administering federal and state grants and loans to students. The majority of the Board is either appointed by the Governor or are State officials. TSAC's budget is approved by the State.
2. The Community Services Agencies (CSAs) (Governmental Fund Types) listed below are to provide a mechanism to facilitate the provision of services for children and other citizens in need of services from state agencies:

Davidson County Community Services Agency  
Knox County Community Services Agency  
Shelby County Community Services Agency  
Hamilton County Community Services Agency  
Northeast Community Services Agency  
East Tennessee Community Services Agency  
Upper Cumberland Community Services Agency  
Southeast Community Services Agency  
Mid-Cumberland Community Services Agency  
South Central Community Services Agency  
Northwest Community Services Agency  
Southwest Community Services Agency

The Boards for these CSAs are appointed by the Governor and the budget must be approved by the State.

3. TN 200 (Governmental Fund Type) was formed to develop a comprehensive program for celebrating the bicentennial of the State. The Board is comprised of State officials and appointees by the Governor, and the State provides a substantial amount of funding. This organization dissolved during fiscal year 1999.
4. The Tennessee Certified Cotton Growers Organization (Governmental Fund Type) was formed to aid in the eradication of the Boll Weevil. The majority of the Board is appointed by the Commissioner of the Department of Agriculture, and the State provides a substantial amount of funding.
5. The Tennessee Housing Development Agency (Proprietary Fund Type) is responsible for making loans and mortgages to qualified sponsors, builders, developers and purchasers of low and moderate income family dwellings. The Board of the agency is appointed by the Governor and its budget is approved by the State.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

6. The Tennessee Local Development Authority (Proprietary Fund Type) provides financing assistance to local governments through the issuance of bonds and notes. In addition, the Authority assists non-profit corporations in the construction of mental health, mental retardation, or alcohol and drug facilities. The majority of the Board consists of State officials; therefore, the State can impose its will on the Authority.
7. The Tennessee Commodity Producer Indemnity Board (Grain Indemnity) (Proprietary Fund Type) is responsible for administering the grain indemnity fund. This fund receives monies from assessments on the sale of grain by producers. These monies are then used to compensate any claimant who has incurred a financial loss due to a failure of a commodity dealer or warehouseman. The Board is comprised of state officials and the State may impose its will since the State appoints, hires and dismisses those individuals responsible for the day-to-day management of the organization.
8. The Tennessee State Veterans' Homes Board (Proprietary Fund Type) is responsible for the operation of nursing homes for honorably discharged veterans of the United States armed forces. The Board is appointed by the Governor and its budget is approved by the State. In addition, the issuance of bonds must be approved by the State Funding Board.
9. The Child Care Facilities Corporation (Proprietary Fund Type) purpose is to create new child care slots in Tennessee by guaranteeing loans, making direct loans, and making grants. The Board is comprised primarily of State officials. The State must approve the budget of the Corporation.
10. The Tennessee State School Bond Authority (Proprietary Fund Type) finances projects for the University of Tennessee, Tennessee Board of Regents or the Tennessee Student Assistance Corporation. The Board of the Authority consists primarily of State officials; therefore, the State is able to impose its will on the organization.
11. The University of Tennessee Board of Trustees (College and University Fund Type) is responsible for the operation of the University of Tennessee, located primarily on four campuses across the State. The Board is appointed by the Governor and the State provides a substantial amount of the funding.
12. The Tennessee Board of Regents (College and University Fund Type) is responsible for the operation of six universities, twelve community colleges, two technical institutes and twenty-seven technology centers. The Board is comprised of State officials and appointees by the Governor and the State provides a substantial amount of funding.

Complete financial statements for each of the individual component units may be obtained at the following addresses:

Tennessee Housing Development Agency  
1114 Parkway Towers  
404 James Robertson Parkway  
Nashville, TN 37243

Tennessee Local Development Authority  
Suite 1600, James K. Polk Building  
Nashville, TN 37243

Tennessee State Veterans' Homes Board  
345 Compton Road  
Murfreesboro, TN 37130

Tennessee State School Bond Authority  
Suite 1600, James K. Polk Building  
Nashville, TN 37243

University of Tennessee  
Office of the Treasurer  
301 Andy Holt Tower  
Knoxville, TN 37996-0100

Tennessee Board of Regents  
1415 Murfreesboro Road, Suite 350  
Nashville, TN 37217

All others may be obtained at the following address:

Finance & Administration  
Division of Accounts  
15th Floor Andrew Jackson Building  
Nashville, TN 37243-0298

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

- C. Fund Structure and Basis of Accounting - The financial activities of the state reported in the accompanying statements are classified into three fund categories and two account groups, all described below. The fund categories include governmental funds, proprietary funds and fiduciary funds. Account groups are presented for general fixed assets and general long-term obligations.

The state's governmental fund types include:

1. the General Fund - used to account for all financial transactions not required to be accounted for in other funds;
2. the Special Revenue Funds - used to account for specific revenues earmarked to finance particular or restricted programs and activities;
3. the Debt Service Fund - used to account for the payment of principal and interest on general long-term debt; and
4. the Capital Projects Fund - used to account for the acquisition or construction of all major governmental capital facilities.

All of the governmental funds are accounted for on the modified accrual basis of accounting. Under this basis, revenues are recognized when they become susceptible to accrual; that is, when they become both measurable and available to finance expenditures of the current period. Principal revenue sources accounted for on the modified accrual basis include federal grants, departmental services, interest on investments, sales taxes, petroleum and vehicular-related taxes and fees, and gross receipts taxes. Licenses, fines, fees and permits are accounted for on the cash basis. Expenditures are recognized when the related fund liability is incurred except:

- a. Inventories generally are considered expenditures when consumed;
- b. Prepayments usually are not recorded; and
- c. Principal and interest on long-term debt are recorded when due.

Encumbrance accounting is utilized for budgetary control purposes in governmental fund types. Encumbrances outstanding at year-end are reported as reservations of fund balance for subsequent year expenditure.

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. All governmental funds and expendable trust funds are accounted for using a current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

The proprietary funds include:

1. the Enterprise Funds - used to account for the operations of self-sustaining state agencies providing goods or services to the general public on a user-charge basis; and
2. the Internal Service Funds - used to account for the operations of self-sustaining state agencies providing goods or services to other state agencies on a cost-reimbursement basis.

The proprietary funds are accounted for on the accrual basis. Under this method, revenues are recorded when earned and expenses at the time liabilities are incurred.

The fiduciary funds represent Trust and Agency Funds which are used to account for assets held by the state in a trust or agency capacity. These funds include:

1. the Expendable Trust Funds - used to account for the activities of trusts whose principal and income may be used for the purposes of the trust;
2. the Nonexpendable Trust Funds - used to account for the activities of trusts whose income is used to fund the trust purpose but whose principal is to be maintained intact;
3. the Pension Trust Fund - used to account for the activities of the state-administered retirement system;
4. Investment Trust Fund – used to account for the activities of the state sponsored external investment pool; and
5. the Agency Funds - used to account for amounts held in custody for others. Agency funds are custodial in nature and do not present results of operations or have a measurement focus.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

Expendable Trust and Agency Funds are accounted for on the modified accrual basis of accounting. Nonexpendable, Pension Trust and Investment Trust Funds are accounted for on the accrual basis.

All proprietary funds, nonexpendable trust funds, pension trust and investment trust funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. Fund equity (i.e., net total assets) is segregated into contributed capital and retained earnings components. Proprietary fund-type operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets.

The financial statements of the pension plans are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. The state's contributions are recognized when due and a formal commitment to provide the contributions has been made. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

The account group for general fixed assets is maintained to account for all fixed assets acquired or constructed for use by the state, other than those accounted for in the proprietary funds.

The account group for general long-term obligations is maintained to account for general obligation bonds outstanding, arbitrage payable, claims payable and accrued annual and compensatory leave not otherwise recorded in proprietary or fiduciary funds.

In addition to the forementioned fund categories and account groups, the component units also include colleges and universities which are accounted for using a different accounting and reporting model.

The college and university fund types (component units - discrete) include:

1. Current Funds - used to account for resources that will be expended in the near term for operating purposes of the institutions. These include (a) unrestricted funds over which the governing boards retain full control in achieving the institutions' purposes and (b) restricted funds which may be utilized only in accordance with externally-restricted purposes;
2. Fiduciary Funds - used to account for assets held by loan, endowment, life income and agency funds in which the universities act in a fiduciary capacity; and
3. Plant Funds - used to account for institutional property acquisition, renewal, replacement, debt service and investment.

The college and university fund types are accounted for on the accrual basis of accounting with the following exceptions:

- A. Depreciation expense related to plant fund assets is not recorded; and
- B. Revenues and expenditures of an academic term encompassing more than one fiscal year are solely reported in the fiscal year in which the term is predominantly conducted.

- D. Proprietary Activity Accounting and Financial Reporting - Activities accounted for in the state's proprietary, non-expendable trust and pension trust funds and proprietary type component units follow all applicable GASB pronouncements as well as applicable private sector pronouncements issued on or before November 30, 1989.
- E. College and University Accounting and Financial Reporting Model - The state uses the AICPA college guide model for accounting and reporting guidance for its colleges and universities, which are presented as component units-discrete.
- F. Budgetary Process - Legislation requires the Governor to present his proposed budget to the General Assembly at the beginning of each annual session. Annual budgets are adopted for the general and special revenue funds, except the Supreme Court Boards, Fraud and Economic Crime and Dairy Promotion Board (accounted for as Special Revenue Funds). The General Assembly enacts the budget through passage of specific departmental appropriations, the sum of which may not exceed estimated revenues. Before signing the Appropriations Act, the Governor may veto or reduce any specific appropriation, subject to legislative override. Once passed and signed, the budget becomes the state's financial plan for the coming year.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

Budgetary control is maintained at the departmental level. Budget revisions during the year, reflecting program changes or intradepartmental transfers of an administrative nature, may be affected with certain executive and legislative branch approval. Only the legislature, however, may transfer appropriations between departments.

Unencumbered appropriations lapse at the end of each fiscal year, with the encumbered appropriations being carried forward to the next year. In order to provide sufficient funding for several programs during the year, supplemental appropriations of \$56.1 million were required.

The state's annual budget is prepared on the modified accrual basis of accounting with several exceptions, principally the effect of encumbrance and contract obligations. Because these exceptions represent departures from generally accepted accounting principles (GAAP), actual amounts in the accompanying budgetary comparison statement are presented on the budgetary basis. A reconciliation of the differences between the budgetary and GAAP basis is presented in Note 2B. The budgetary comparison statement includes the General Fund and all budgeted Special Revenue Funds.

G. Cash and Cash Equivalents - This classification includes demand accounts, petty cash and monies in cash management pools. The liquidity of the cash management pools is sufficient to cover any withdrawal request by a participant. This classification also includes short-term investments with a maturity date within three months of the date acquired by the state. These short-term investments, which are not part of the State Cash Pool, are stated at fair value. Investments in the State Cash Pool are stated at cost or amortized cost as this pool is a 2a7-like pool. Collateral, as required by law, is pledged by the various banks and government securities dealers to guarantee state funds placed with them. It is the state's policy to include cash management pools as cash. In addition, all securities whose primary purpose is to facilitate the placement of funds in long-term investment vehicles are classified as investments.

H. Investments - This classification includes long-term investments which are stated at fair value.

Securities traded on a national or international exchange are valued at the last reported sales price at current exchange rates. Investments that do not have an established market are reported at estimated fair values. Investment income consists of realized and unrealized appreciation in the fair value of investments. Interest income is recognized when earned. Securities and security transactions are recorded in the financial statements on trade-date basis.

I. Receivables - Receivables in the state's governmental and fiduciary funds primarily consist of taxes, interest, departmental services and federal revenues, recorded when earned. The remaining governmental fund revenues are not considered susceptible to accrual prior to receipt; accordingly, licenses, fees, fines, permits and similar revenues are recognized on the cash basis. Certain Trust Fund receivables, representing taxes and benefits overpayments, have been reduced by an allowance for uncollectibles. Receivables in all other funds have arisen in the ordinary course of business. College and University receivables have also been reduced by an uncollectible allowance.

J. Interfund Transactions - The state basically has four types of interfund transactions, as follows:

1. Services rendered and employee benefit contributions. These transactions are accounted for as revenues, expenditures or expenses in the funds involved.
2. Operating appropriations/subsidies. These are accounted for as operating transfers in the funds involved.
3. Equity contributions. These are accounted for as equity transfers (additions to or deductions from beginning governmental fund balances or proprietary fund contributed capital).
4. College and university interfund borrowings. These transactions represent borrowings of a temporary nature and are reported as assets of the college and university fund making the advance and as liabilities of the fund receiving the advance.

The composition of the state's due to/from other funds at June 30, 1999 is presented in Note 2E.

K. Advances to Other Funds - Noncurrent portions of long-term interfund loan receivables are reported as advances and are offset equally by a fund balance reserve account which indicates that they do not constitute expendable available financial resources and therefore are not available for appropriation.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

- L. Inventories - Inventories of materials and supplies are determined by physical count and are valued at cost, principally using the first-in/first-out (FIFO) method. The average cost method is used for the Highway Fund (a Special Revenue Fund) and Motor Vehicle Management (an Internal Service Fund). The costs of governmental fund-type inventories are recorded as expenditures when consumed rather than when purchased.
- M. Fixed Assets and Depreciation - General fixed assets are presented in the accompanying financial statements at cost or estimated historical cost. Donated fixed assets are stated at fair market value at the time of donation. Interest during construction has not been capitalized. Also, certain public domain fixed assets (including highways, bridges, highway lands and rights-of-way) are not capitalized. No depreciation is provided on general fixed assets.

Enterprise, Internal Service and Nonexpendable Trust Fund fixed assets are stated at cost or estimated historical cost. Donated fixed assets are stated at fair market value at the time of donation. They are being depreciated principally on a straight-line basis over estimated useful lives ranging from 20 to 50 years for Structures and Improvements and 4 to 20 years for Machinery and Equipment. It is the state's policy to capitalize interest expense incurred on significant assets during their construction.

A statement of changes in general fixed assets for the year ended June 30, 1999 is presented in Note 2A.

Generally, College and University component units fixed assets are stated at cost and are not depreciated. Donated fixed assets are stated at fair market value at the time of donation. Because of the magnitude of library holdings, however, it has been the state's policy to value library books at a standard amount per volume, currently \$48, which approximates current cost.

- N. Accumulated Unpaid Vacation and Sick Pay - The state's liability for accumulated unpaid annual and compensatory time is reported in the accompanying General Long-Term Obligations Account Group for all governmental fund types. In the proprietary fund types and the college and university fund types, this obligation is reported as a fund liability.

There is no liability in the accompanying financial statements for unpaid accumulated sick leave since it is the state's policy to record the cost of sick leave only when paid. This contingency amount is disclosed in Note 9A.

- O. Fiscal Year End - The fiscal year end of the primary government and component units is June 30, except for the following agencies reported as Special Revenue funds: Supreme Court Boards and Dairy Promotion Board. Both of these organizations have a December 31 year end, and UHS Ventures, Inc. (a component unit of the University of Tennessee), also has a December 31 year end.

- P. Fund Balance Reserves and Designations - The state's fund balance reserves represent those portions of fund balance (1) not appropriable for expenditure or (2) legally segregated for a specific future use. In the accompanying Combined Balance Sheet, reserves for related assets such as inventories, petty cash, advances, long-term receivable, and prepayments are examples of the former. Reserves for encumbrances, contracts, continuing appropriations and other specific purposes are examples of the latter. The state's fund balance designations reflect tentative plans for future use of financial resources. The General Fund designation for revenue fluctuations, has been established as protection in the event of future revenue shortfalls or expenditure overruns.

- Q. Totals (Memorandum Only) - Total columns on the general-purpose financial statements are captioned "memorandum only" to indicate that they are presented only to facilitate financial analysis. Data in these columns do not present financial position, results of operations or cash flows in conformity with generally accepted accounting principles. Neither are such data comparable to a consolidation. Interfund eliminations have not been made in the aggregation of this data.

- R. Comparative Data - Comparative total data for the prior year have been presented in the accompanying financial statements in order to provide an understanding of changes in the government's financial position and operations. However, comparative data have not been presented in all statements because their inclusion would make certain statements unduly complex and difficult to understand.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

**NOTE 2 - OTHER ACCOUNTING DISCLOSURES**

- A. General Fixed Assets - A statement of changes in general fixed assets for the year ended June 30, 1999 is shown below (expressed in thousands).

	<u>Land</u>	<u>Structures and Improvements</u>	<u>Machinery and Equipment</u>	<u>Construction in Progress</u>	<u>Totals</u>
Balance, July 1, 1998	\$154,293	\$1,079,658	\$345,828	\$ 102,674	\$ 1,682,453
Additions	16,653	94,964	70,872	40,736	223,225
Deductions	<u>(3,982)</u>	<u>(858)</u>	<u>(35,677)</u>	<u>(92,696)</u>	<u>(133,213)</u>
Balance, June 30, 1999	<u>\$166,964</u>	<u>\$1,173,764</u>	<u>\$381,023</u>	<u>\$ 50,714</u>	<u>\$1,772,465</u>

- B. Budgetary Basis vs. GAAP - The accompanying Combined Statement of Revenues, Expenditures and Changes in Fund Balances - Budget and Actual - General Fund and All Budgeted Special Revenue Fund Types presents comparisons of the legally adopted budget with actual data on a budgetary basis. Since the budgetary and GAAP presentations of actual data differ, a reconciliation of the two is presented below (expressed in thousands).

	<u>General Fund</u>	<u>All Special Revenue Funds</u>
Fund Balances (Budgetary Basis), June 30, 1999	\$ 539,013	\$ 192,624
Add:		
Reserve for encumbrances and contracts	8,272	222,807
Highway construction appropriations carried forward		132,826
Unbudgeted Supreme Court Boards		2,276
Unbudgeted Dairy Promotion Board		4
Unbudgeted Fraud and Economic Crime		<u>1,718</u>
Fund Balances (GAAP Basis), June 30, 1999	<u>\$ 547,285</u>	<u>\$ 552,255</u>

- C. Fund Equity Restatement/Change in Accounting Principle

Change in Accounting Principle: During fiscal year 1999, the State implemented a new accounting standard (GASB Statement 32). Based on revisions to the law, this statement rescinded the requirement to account for IRC Section 457 deferred compensation plans in an agency fund of the employer. The laws governing these plans were changed to require that all assets and income of the 457 plan be held in trust. The State established the Deferred Compensation Plan and Trust. The effect of this change is to eliminate the Deferred Compensation agency fund.

Prior Period Adjustments: The Capital Projects Fund (CPF) has a prior period adjustment because of a change in accounting for capital expenditures of capital projects that are reported in the Facilities Revolving Fund (FRF), an internal service fund. In essence, debt proceeds and capital expenditures are reported in the FRF instead of the CPF. The effect of this adjustment on the prior year Statement of Revenues, Expenditures, and Changes in Fund Balance is a reduction of Excess of Revenues and Other Sources Over (Under) Expenditures and Other Uses in the amount of \$5.5 million.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

D. Segment Information - Segment financial information for the state's Enterprise Funds for the year ended June 30, 1999, is presented below (expressed in thousands). These enterprise funds provide the following types of goods or services (in the order shown below): Sewage treatment loans, sewage treatment facilities loans, energy loans, insurance, insurance, drinking water system loans, and property distribution.

	<u>State Loan</u> <u>Program</u>	<u>Sewer</u> <u>Treatment</u> <u>Loan</u>	<u>Energy Loan</u> <u>Program</u>
Operating Revenues	\$ 1,199	\$ 13,555	\$ 739
Depreciation and Amortization	10		
Operating Income (Loss)	(92)	13,555	739
Operating Grants, Entitlements, and Shared Revenues		816	203
Operating Transfers In			
Operating Transfers Out to Component Units	25		
Net Income (Loss)	(117)	13,555	942
Current Capital Transfers		19,320	
Equity Transfers In		3,758	
Property, Plant and Equipment:			
Additions			
Deletions			
Net Working Capital	2,970	106,659	13,779
Total Assets	28,164	349,737	16,875
Bonds and Other Long-Term			
Liabilities Payable from			
Operating Revenues	20,356		
Total Equity	3,781	349,727	16,875

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

<u>Teacher Group Insurance</u>	<u>Local Government Group Insurance</u>	<u>Drinking Water</u>	<u>Property Utilization</u>	<u>Totals</u>
\$ 122,491	\$ 37,503	\$ 251	\$ 1,328	\$ 177,066
(6,371)	2,200	251	6	16
		180	(256)	10,026
2,051			200	1,199
(3,392)	2,884	251	(56)	2,251
		1,254		25
		3,970		14,067
			2	20,574
1,694	10,853	6,479	14	7,728
20,070	14,828	8,147	315	2
			444	14
				142,749
				438,265
				20,356
1,694	10,853	8,147	317	391,394

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

E. Due To/Due From Other Funds - A summary of due from other funds and due to other funds at June 30, 1999 is shown below (expressed in thousands).

DUE FROM OTHER FUNDS				
		<u>Special Revenue</u>	<u>Internal Service</u>	<u>Trust and Agency Funds</u>
<u>DUE TO OTHER FUNDS</u>	<u>General Fund</u>	<u>Education</u>	<u>Office for Information Resources</u>	<u>Employment Security</u>
General		\$ 989	\$ 525	\$ 83
Special Revenue:				
Education Trust	\$ 248,783			
Highway				
Wildlife Resources				
Agency				
Solid Waste				
Hazardous Waste				
Underground Storage				
Tanks				
Enhanced Emergency 911 Service				
Driver Education				
Salvage Title				
Enforcement				
Drycleaner's Environmental				
Response				
Tennessee Regulatory Authority				
Enterprise:				
Property Utilization				
Internal Service:				
Office for Information				
Resources				
Motor Vehicle				
Management				
General Services				
Printing				
Food Services				
Postal Services	465			
Purchasing				
Central Stores	3			
Records Management				
Trust and Agency:				
Chairs of Excellence	59			
Totals	\$ 249,310	\$ 989	\$ 525	\$ 83

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

DUE FROM OTHER FUNDS

Trust and Agency Funds

<u>Employee Flexible Benefits</u>	<u>Baccalaureate Education</u>	<u>Pension Trust</u>	<u>Contingent Revenue</u>	<u>Totals</u>
\$ 50	\$ 7	\$ 1,918	\$ 5,377	\$ 8,949
3		61	173	249,020
		257	725	982
		45	122	167
		2	4	6
		5	13	18
1		5	15	21
			1	1
			1	1
		1	2	3
		1	1	2
1		6	18	25
		2	4	6
2	1	29	80	112
		2	6	8
		3	8	11
			1	1
		3	7	475
		3	8	11
		1	3	7
		1	4	5
				59
<u>57</u>	<u>8</u>	<u>2,345</u>	<u>6,573</u>	<u>259,890</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

F. Due to Primary Government From Component Units - A summary of due to the primary government from the component units at June 30, 1999 is shown below (expressed in thousands).

	<u>DUE FROM COMPONENT UNITS</u>						
	<u>General</u>	<u>Special Revenue Funds</u>	<u>Capital Projects</u>	<u>Enterprise Funds</u>		<u>Internal Service Funds</u>	
		<u>Education</u>		<u>Local Govt. Group Insc.</u>	<u>Property Utiliz.</u>	<u>Office for Information Resources</u>	<u>Claims Award</u>
<u>DUE TO PRIMARY GOVERNMENT</u>							
TN Student Assistance Corporation							
Northeast CSA	\$ 241					\$ 10	
East TN CSA	103						
Upper Cumberland CSA	30					39	
Southeast CSA	234			\$ 1		9	
Mid-Cumberland CSA	124					13	
South Central CSA	370					5	
Northwest CSA	226					7	
Southwest CSA	362					6	
Davidson Co. CSA	39						
Knox Co. CSA	294				3	3	
Shelby Co. CSA	31						
Hamilton Co. CSA	50					7	
Tennessee Housing Development Agency	121						
Veteran's Nursing Home	1,011						\$ 28
Board of Regents	1,861	\$ 23	\$ 1,612		\$ 3	461	
University of Tennessee	115					1	35
	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>	<u>          </u>
Totals	<u>\$ 5,212</u>	<u>\$ 23</u>	<u>\$ 1,612</u>	<u>\$ 4</u>	<u>\$ 4</u>	<u>\$ 595</u>	<u>\$ 28</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

DUE FROM COMPONENT UNITS

<u>Internal Service Funds</u>			<u>Trust and Agency Funds</u>					
<u>Motor Vehicle Management</u>	<u>Facilities Revolving Fund</u>	<u>Central Stores</u>	<u>Employment Security</u>	<u>Employee Flexible Benefits</u>	<u>Chairs of Excellence</u>	<u>Pension Trust</u>	<u>Contingent Revenue</u>	<u>Totals</u>
						\$ 1	\$ 5	\$ 6
			\$ 1			14		266
								103
						6		75
			1			5		250
			2			8		147
			1			7		383
			2			13		248
								368
								39
			1					301
								31
			1			6		64
				\$ 1		9	26	157
			6			8		1,053
\$ 35	\$ 3	\$ 1				1,154		5,153
2		1			\$ 460	8		622
<u>37</u>	<u>3</u>	<u>2</u>	<u>15</u>	<u>1</u>	<u>460</u>	<u>1,239</u>	<u>31</u>	<u>9,266</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

G. Due From Primary Government To Component Units - A summary of due to the component units from the primary government at June 30, 1999 is shown below (expressed in thousands).

<u>DUE FROM PRIMARY GOVERNMENT</u>	<u>DUE TO COMPONENT UNITS</u>				<u>Totals</u>
	<u>General</u>	<u>Capital Projects</u>	<u>Local Government Group Insurance</u>	<u>Chairs of Excellence</u>	
Northeast CSA	\$ 302				\$ 302
East TN CSA	289				289
Upper Cumberland CSA	114				114
Mid-Cumberland CSA	356		\$ 6		362
South Central CSA	111				111
Northwest CSA	165				165
Southwest CSA	87				87
Davidson County CSA	110				110
Knox County CSA	95				95
Shelby County CSA	432				432
Tennessee Board of Regents	14			\$ 1,501	1,515
University of Tennessee	<u>          </u>	<u>\$ 1,886</u>	<u>          </u>	<u>1,138</u>	<u>3,024</u>
Total	<u>\$ 2,075</u>	<u>\$ 1,886</u>	<u>\$ 6</u>	<u>\$ 2,639</u>	<u>\$ 6,606</u>

H. Discretely Presented Component Unit – The University of Tennessee Balance Sheet includes Due From and Due To Other Funds of \$11.849 million and \$10.121 million respectively. The \$1.728 million difference is a result of reporting transactions between the University of Tennessee and UHS Ventures, Inc. Due to the controlled governance by the university, UHS Ventures, Inc. must be presented as a component unit of the University of Tennessee. The transactions between the university and UHS Ventures, Inc. do not agree in the accompanying financial statements because they have different fiscal year ends. All activity reported for UHS Ventures, Inc. is as of and for the year ended December 31, 1998.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

I. Due to Component Units From Component Units - A summary of due to the component units from component units at June 30, 1999 is shown below (expressed in thousands).

DUE FROM COMPONENT UNITS	DUE TO COMPONENT UNITS				<u>Totals</u>
	<u>Northwest CSA</u>	TN State School Bond <u>Authority</u>	Board of <u>Regents</u>	University of <u>Tennessee</u>	
Southwest CSA	\$ 1				\$ 1
TN State School Bond Authority			\$ 7,293	\$ 14,367	21,660
University of Tennessee		\$ 1,564			1,564
TN Board of Regents		4,091			4,091
Totals	<u>\$ 1</u>	<u>\$ 5,655</u>	<u>\$ 7,293</u>	<u>\$ 14,367</u>	<u>\$27,316</u>

J. Advances -

The General Fund has an advance of \$190 thousand to a component unit, the Veterans' Homes Board. The Veterans' Homes Board is to repay the advance out of profits generated.

Tennessee State School Bond Authority has made the following advances to other component units (expressed in thousands):

	<u>Advances from Component Units</u>
Tennessee Board of Regents	\$ 145,140
University of Tennessee	<u>292,870</u>
	<u>\$ 438,010</u>

These advances are due in varying amounts annually and are sufficient to pay the debt service on the bonds and notes payable that the Tennessee State School Bond Authority has issued.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

K. Accounts and Notes Receivable - Receivables at June 30, 1999 consist of the following (expressed in thousands):

	<u>General</u>	<u>Special Revenue</u>	<u>Debt Service</u>	<u>Capital Projects</u>	<u>Enterprise</u>	<u>Internal Service</u>	<u>Trust and Agency</u>	<u>Total</u>
Accounts Receivable:								
Interest	\$ 17,972				\$ 4		\$212,475	\$ 230,451
Taxes	344,651	\$ 347,191	\$ 3,430				241,408	936,680
Accounts	12,842	348			7,517	\$ 3,102	159,865	183,674
Intergovernmental	<u>386,027</u>	<u>116,754</u>	<u>      </u>	<u>\$ 1,278</u>	<u>279,113</u>	<u>2</u>	<u>2,918</u>	<u>786,092</u>
Gross Accounts Receivable	761,492	464,293	3,430	1,278	286,634	3,104	616,666	2,136,897
Less: Allowance for Uncollectibles	<u>      </u>	<u>      </u>	<u>      </u>	<u>      </u>	<u>      </u>	<u>      </u>	<u>(20,488)</u>	<u>(20,488)</u>
Net Accounts Receivable	<u>\$761,492</u>	<u>\$ 464,293</u>	<u>\$ 3,430</u>	<u>\$ 1,278</u>	<u>\$ 286,634</u>	<u>\$ 3,104</u>	<u>\$596,178</u>	<u>\$2,116,409</u>

Component Units

	<u>Tennessee Student Assistance Corporation</u>	<u>Tennessee Housing Development Agency</u>	<u>Tennessee Local Development Authority</u>	<u>Board of Regents</u>	<u>University of Tennessee</u>	<u>Other</u>	<u>Total</u>
Accounts Receivable:							
Interest	\$ 271	\$ 18,517	\$ 73	\$ 3,489			\$ 22,350
Accounts	20,826	1,249,376	87,288	62,012	\$ 191,841	\$ 2,414	1,613,757
Intergovernmental	<u>1,166</u>	<u>      </u>	<u>      </u>	<u>      </u>	<u>      </u>	<u>      </u>	<u>1,166</u>
Gross Accounts Receivable	22,263	1,267,893	87,361	65,501	191,841	2,414	1,637,273
Less: Allowance for Uncollectibles	<u>      </u>	<u>      </u>	<u>      </u>	<u>(7,693)</u>	<u>(47,986)</u>	<u>      </u>	<u>(55,679)</u>
Net Accounts Receivable	<u>\$ 22,263</u>	<u>\$ 1,267,893</u>	<u>\$ 87,361</u>	<u>\$ 57,808</u>	<u>\$ 143,855</u>	<u>\$ 2,414</u>	<u>\$ 1,581,594</u>
Notes Receivable	\$ 5,880			\$ 28,542	\$ 35,036		\$ 69,458
Less: Allowance for Uncollectibles	<u>      </u>	<u>      </u>	<u>      </u>	<u>(6,305)</u>	<u>(1,203)</u>	<u>      </u>	<u>(7,508)</u>
Net Notes Receivable	<u>\$ 5,880</u>	<u>      </u>	<u>      </u>	<u>\$ 22,237</u>	<u>\$ 33,833</u>	<u>      </u>	<u>\$ 61,950</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

L. Fund Balance Reserves and Designations - Specific purpose reserves represent current and past legislative appropriations requiring year-end segregation. A summary of the nature and purpose of these reserves at June 30, 1999 by fund type follows (expressed in thousands).

<u>Reserved for Other Specific Purposes</u>	<u>General</u>	<u>Special Revenue</u>	<u>Trust and Agency</u>
Highway Construction		\$132,826	
Wildlife Resources Program		31,276	
Criminal Injuries Compensation		64,550	
Solid Waste		7,595	
Job Skills		11,001	
Environmental Protection		11,364	
Hazardous Waste Program		9,026	
Parks Acquisition		17,609	
Unemployment Compensation Benefits			\$ 955,601
Pension Benefits			22,797,512
Higher Education Chairs of Excellence			226,415
Local Government Investment Pool			1,571,585
Probation Supervision and Rehabilitation	\$ 4,142		
Commerce and Insurance Regulatory Boards	2,954	2,862	
Health Regulatory Boards	2,747		
Traumatic Brain Injury	1,356		
Sports Authority	1,471		
Temporary Assistance	6,524		
Alcohol Drug Addition Treatment	1,246		
Other Non-Lapsing and Special Revenue Programs	<u>11,266</u>	<u>23,730</u>	<u>17,288</u>
Totals	<u>\$ 31,706</u>	<u>\$ 311,839</u>	<u>\$25,568,401</u>

The General Fund designation for other specific purposes represents the following appropriations made by the Legislature to carry out tentative managerial plans for fiscal year 2000 (expressed in thousands):

Future Appropriations	\$ 89,500
Casualty Losses	8,219
Industries for the Blind	<u>132</u>
	<u>\$ 97,851</u>

The reserve for related assets represents assets which are not available for appropriation. A summary of these reserves at June 30, 1999 by fund type follows (expressed in thousands).

<u>Reserved for Related Assets</u>	<u>General</u>	<u>Special Revenue</u>
Inventories		\$ 6,679
Advances to Component Units	\$ 190	
Long-Term Receivables	2,987	
Prepayments	24	13
	<u>\$ 3,201</u>	<u>\$ 6,692</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

- M. Related Organizations - The State's officials are also responsible for appointing the members of the boards of other organizations, but the State's accountability for these organizations does not extend beyond making appointments. The State appoints the board members of the Beech River Watershed Development Authority, Carroll County Watershed Authority, Goodwyn Institute Commission, Watkins Institute Commission, Tennessee Alliance for Fitness and Health, Tennessee Competitive Export Corporation, Insurance Guaranty Association, Tennessee Sports Hall of Fame, Local Neighborhood Development Corporations, Tennessee Holocaust Commission, Inc., and Sports Festival, Inc.
- N. Joint Ventures -The State is a participant in a joint venture, the Tennessee-Tombigbee Waterway Development Compact, with the states of Alabama, Kentucky and Mississippi. The purpose of this compact is to promote the development of a navigable waterway connecting the Tennessee and Tombigbee Rivers and provide a nine foot navigable channel. The fiscal year end of the Tennessee Tombigbee Waterway is December 31. Financial statements for the Tennessee Tombigbee Waterway may be obtained at: P. O. Drawer 671, Columbus, MS 39703.

Presented below is summary financial data for this joint venture (expressed in thousands):

	<u>1998</u>	<u>1997</u>
Current Assets	\$ 310	\$ 278
Property Plant & Equipment	<u>25</u>	<u>19</u>
Total Assets	<u>335</u>	<u>297</u>
Current Liabilities		2
Investment in General Fixed Assets	25	19
Fund Balance	<u>310</u>	<u>276</u>
Total Liabilities and Fund Balance	<u>335</u>	<u>297</u>
Revenues	320	359
Expenditures	<u>286</u>	<u>275</u>
Excess of Revenues over (under) expenditures	34	84
Beginning Fund Balance	<u>276</u>	<u>192</u>
Ending Fund Balance	<u>\$ 310</u>	<u>\$ 276</u>

- O. Jointly Governed Organizations - The State in conjunction with 26 other states are members of the Pest Control Compact.

The State in conjunction with 13 other states are members of the Southern Growth Policies Board. Tennessee paid some \$40,917 in fiscal year 1999 for membership dues.

The Southern Regional Education Compact was entered into with 14 other states. Tennessee paid \$8,240 in dues in fiscal year 1999.

The Compact for Education was entered into with 49 other states.

The Interstate Mining Compact has 17 member states, including Tennessee. Tennessee paid \$12,028 in fiscal year 1999 for membership dues.

The Southern States Energy Board is comprised of 16 member states, including Tennessee.

The Southeast Interstate Low Level Radioactive Waste Compact has 7 member states.

The Chickasaw Trail Economic Development Compact has two member states in conjunction with one county in each state.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

P. Presented below are the condensed financial statements for the discretely presented component units (expressed in thousands):

CONDENSED FINANCIAL STATEMENTS - DISCRETELY PRESENTED COMPONENT UNITS

BALANCE SHEETS

	Tennessee Student Assistance Corporation	Tennessee Housing Develop. Agency	Tennessee Local Develop. Authority	Tennessee State School Bond Authority	Tennessee Board of Regents	University of Tennessee	Other	Total
<b>Assets:</b>								
Current Assets	\$ 89,991	\$ 462,310	\$ 35,247	\$ 24,800	\$ 333,332	\$ 522,575	\$ 21,467	\$1,489,722
Due from Primary Government					1,515	3,024	2,067	6,606
Due from Component Units				21,660	4,091	1,564	1	27,316
Advance to Component Units				438,010				438,010
Other Assets		1,647,016	90,120	27,759	142,356	467,707	202	2,375,160
Fixed Assets	145	110			1,995,976	1,913,013	12,355	3,921,599
Amounts to be Provided	85						1,038	1,123
<b>Total Assets</b>	<u>\$ 90,221</u>	<u>\$ 2,109,436</u>	<u>\$ 125,367</u>	<u>\$ 512,229</u>	<u>\$2,477,270</u>	<u>\$ 2,907,883</u>	<u>\$ 37,130</u>	<u>\$8,259,536</u>
<b>Liabilities:</b>								
Current Liabilities	\$ 7,814	\$ 145,226	\$ 51,501	\$ 170,489	\$ 226,581	\$ 207,560	\$ 8,292	\$ 817,463
Due to Primary Government	6	157			5,153	622	3,328	9,266
Due to Component Units				5,655	7,293	14,367	1	27,316
Bonds Payable		1,634,858	62,813	329,562	1,467		5,040	2,033,740
Advance From Primary Government							190	190
Advance from Component Units					145,140	292,870		438,010
<b>Total Liabilities</b>	<u>7,820</u>	<u>1,780,241</u>	<u>114,314</u>	<u>505,706</u>	<u>385,634</u>	<u>515,419</u>	<u>16,851</u>	<u>3,325,985</u>
<b>Equity:</b>								
Investment in General Fixed Assets	145				1,845,477	1,605,801	1,851	3,453,274
Contributed Capital		2,500					10,164	12,664
Retained Earnings		326,695	11,053	6,523			2,233	346,504
Fund Balances	<u>82,256</u>				<u>246,159</u>	<u>786,663</u>	<u>6,031</u>	<u>1,121,109</u>
<b>Total Equity</b>	<u>82,401</u>	<u>329,195</u>	<u>11,053</u>	<u>6,523</u>	<u>2,091,636</u>	<u>2,392,464</u>	<u>20,279</u>	<u>4,933,551</u>
<b>Total Liabilities and Equity</b>	<u>\$ 90,221</u>	<u>\$ 2,109,436</u>	<u>\$ 125,367</u>	<u>\$ 512,229</u>	<u>\$2,477,270</u>	<u>\$ 2,907,883</u>	<u>\$ 37,130</u>	<u>\$8,259,536</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

STATEMENTS OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES

	<u>Tennessee Student Assistance Corporation</u>	<u>Other</u>	<u>Total</u>
Revenues	\$ 18,009	\$ 5,434	\$ 23,443
Expenditures:			
Current	33,193	42,111	75,304
Transfers From Primary Government	<u>22,264</u>	<u>38,370</u>	<u>60,634</u>
Excess of Revenues and Other Financing Sources Over (Under) Expenditures	7,080	1,693	8,773
Fund Balances, July 1	75,176	4,421	79,597
Equity Transfers to Primary Government	<u>                    </u>	<u>(83)</u>	<u>(83)</u>
Fund Balances, June 30	<u>\$ 82,256</u>	<u>\$ 6,031</u>	<u>\$ 88,287</u>

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN EQUITY

	<u>Tennessee Housing Develop. Agency</u>	<u>Tennessee Local Develop. Authority</u>	<u>Tennessee School Bond Authority</u>	<u>Other</u>	<u>Total</u>
Operating Revenues	\$ 117,903	\$ 7,779	\$ 24,233	\$ 9,928	\$ 159,843
Operating Expenses	<u>108,913</u>	<u>5,977</u>	<u>23,131</u>	<u>10,050</u>	<u>148,071</u>
Operating Income (Loss)	8,990	1,802	1,102	(122)	11,772
Non-Operating Revenues (Expenses)	6,987			(31)	6,956
Transfers From Primary Government		25			25
Extraordinary Items	<u>(695)</u>	<u>(2,012)</u>	<u>(699)</u>	<u>                    </u>	<u>(3,406)</u>
Net Income (Loss)	15,282	(185)	403	(153)	15,347
Fund Equity, July 1	<u>313,913</u>	<u>11,238</u>	<u>6,120</u>	<u>12,550</u>	<u>343,821</u>
Fund Equity, June 30	<u>\$ 329,195</u>	<u>\$ 11,053</u>	<u>\$ 6,523</u>	<u>\$ 12,397</u>	<u>\$ 359,168</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

STATEMENTS OF CURRENT FUNDS REVENUES, EXPENDITURES AND OTHER CHANGES

	Tennessee Board of <u>Regents</u>	University of <u>Tennessee</u>	<u>Total</u>
Revenues	\$ 676,522	\$ 920,368	\$ 1,596,890
Expenditures:			
Education and General	1,141,229	844,359	1,985,588
Auxiliary Enterprise and Hospital	57,904	385,757	443,661
Transfers To Other Colleges and University Funds	(37,116)	(58,490)	(95,606)
Transfers From Primary Government	557,704	382,703	940,407
Other Additions (Deductions)	<u>2,424</u>	<u>764</u>	<u>3,188</u>
Net Increase (Decrease) in Fund Balances	<u>\$ 401</u>	<u>\$ 15,229</u>	<u>\$ 15,630</u>

Q. Individual Fund Deficits - The following individual funds have deficit retained earnings/fund balances at June 30, 1999 (expressed in thousands):

Enterprise Funds:	
Teacher Group Insurance	\$ (10,906)
Property Utilization	\$ (1,293)
Internal Service Funds:	
Food Services	\$ (2,817)
Central Stores	\$ (130)
Component Units:	
Veteran's Home Board	\$ (1,174)
Child Care Facilities	\$ (158)
University of Tennessee Unexpended Plant	\$ (10,191)

Increases in fees and charges for services and products are expected to eliminate the deficits in these funds in fiscal years 2000 and beyond.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

**NOTE 3 – LONG-TERM LIABILITIES AND CERTAIN OTHER OBLIGATIONS**

A. Bonds Payable - Bonds Payable at June 30, 1999 are shown below (expressed in thousands).

	<u>Bonds</u>
<u>Enterprise Funds:</u>	
General obligation bonds, 5.0%, due in generally decreasing amounts of principal and interest ranging from \$2.6 million in 2002 to \$719 thousand in 2006	\$ 11,980
General obligation refunding bonds, 1996 Series C, 4.6% to 5.0%, principal and interest due in amounts ranging from \$1.8 million in 2000 to \$986 thousand in 2010	<u>11,784</u>
	23,764
Less: Unamortized bond refunding costs	<u>(213)</u>
Total Enterprise Funds	<u>23,551</u>
<u>Internal Service Funds:</u>	
General obligation bonds, 3.4% to 7.4%, due in decreasing amounts of principal and interest from \$15.3 million in 2000 to \$105 thousand in 2019	75,872
General obligation refunding bonds, 1996 Series B, 4.6% to 6%, principal and interest due in amounts ranging from \$1.9 million in 2000 to \$8 thousand in 2011	12,150
General obligation refunding bonds, 1999 Series A, 3.05% to 5%, principal and interest due in amounts ranging from \$2.9 million in 2000 to \$943 thousand in 2015	<u>50,715</u>
	138,737
Less: Unamortized bond refunding costs	<u>(3,456)</u>
Total Internal Service Funds	<u>135,281</u>
<u>General Long-Term Debt:</u>	
General obligation bonds, 3.4% to 7.4%, due in decreasing amounts of principal and interest from \$71 million in 2000 to \$4 million in 2029	585,278
General obligation refunding bonds, 1991 Series A, 6.1% to 6.35%, principal and interest due in amounts ranging from \$6.2 million in 2000 to \$5.6 million in 2002	15,675
General obligation refunding bonds, 1996 Series B, 4.6% to 6%, principal and interest due in amounts ranging from \$20.3 million in 2000 to \$3.9 million in 2011	127,580
General obligation refunding bonds, 1999 Series A, 3.05% to 5%, principal and interest due in amounts ranging from \$16.5 million in 2000 to \$4.5 million in 2015	<u>199,036</u>
Total General Long-Term Debt	<u>927,569</u>
 Total Bonds Payable	 <u>\$1,086,401</u>

Bond sales during the year ended June 30, 1999 included the following issues:

- November 1998 - General obligation bonds of \$65.955 million.
- June 1999 - General obligation bonds of \$95.725 million.
- April 1999 - General obligation refunding bonds of \$247.8 million.

The \$161.68 million general obligation bond issues above represent bonds maturing serially through 2029 at interest rates ranging from 3.8% to 7.4%. Proceeds of \$84.1 million were used to redeem bond anticipation notes.

In April 1999, the state issued general obligation refunding bonds in the amount of \$247.8 million at a premium of \$10 million to provide for the current refunding of \$44.968 million of general obligation bonds issued in February 1987; and the advance refunding of \$60.05 million of general obligation bonds issued in July 1992, \$80.6 million issued in March 1994, and \$55.55 million issued in March 1995. Proceeds for the advance refunding were deposited with the State Treasurer who holds these monies in a trustee capacity; the assets and an offsetting liability are reported in an agency fund. The bonds are considered to be defeased.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

Of the refunding bonds issued, \$48.764 million is payable from the Facilities Revolving Fund, an Internal Service Fund. The carrying amount of the refunded bonds was \$46.998 million and a call premium of \$499 thousand was paid on the redemption. The refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$3.495 million. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations using the straight-line method based on the refunded bonds maturities which range from 2007 to 2015. The refunding was completed to reduce its total debt service payments over the next 15 years by \$1.499 million and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$977 thousand.

Of the refunding bonds issued, \$199.036 million is payable from the Debt Service Fund. The carrying amount of the refunded bonds was \$194.143 million and a call premium of \$2.060 million was paid on the redemption. The refunding was completed to reduce its total debt service payments over the next years by \$6.117 million and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$3.987 million.

In prior years, the state defeased certain general obligation bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and liability for the defeased bonds are not included in the General Long-Term Obligations Account Group. However, since the State Treasurer is holding these monies in a trustee capacity, the assets and an offsetting liability are reported in an agency fund. As of June 30, 1999, \$73 million of bonds outstanding are considered defeased.

B. Notes Payable - Notes payable at June 30, 1999 are shown below (expressed in thousands).

	<u>Notes</u>
<u>General Long-Term Debt:</u>	
General Obligation bond anticipation notes, variable rate, due July 2001	\$ 129,528
<u>Internal Service Funds:</u>	
General Obligation bond anticipation notes, variable rate, due July 2001	<u>31,772</u>
Total Notes Payable	<u>\$ 161,300</u>

The full faith and credit of the state, together with certain tax revenues, are pledged to secure all general obligation bonds and bond anticipation notes listed above. Although the Enterprise (State Loan Program) and Internal Service Fund (Facilities Revolving Fund, Office of Information Resources, Motor Vehicle Management, and Equipment Revolving Fund) general obligation debt is being retired from resources of those funds, the state remains contingently liable for its payment.

In April 1996, the State instituted a general obligation bond anticipation note program for authorized capital projects. Under this program, notes may be issued from time to time as required; however, generally only \$250 million may be outstanding at any time. The notes bear interest for a weekly rate period, and will continue to do so unless adjusted to a different rate period. During the weekly rate period, the notes will be subject to tender for purchase upon notice to the tender agent. The State has entered into a Standby Note Purchase Agreement with the Tennessee Consolidated Retirement System ("TCRS") under which TCRS is obligated to pay the purchase price of any note tendered for optional or mandatory purchase and not remarketed. The obligation of TCRS to purchase tendered unremarketed notes is subject to suspension or termination upon certain events. Unless terminated early, the Standby Note Purchase Agreement will terminate on July 2, 2001, the stated maturity of the program.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

C. Debt Service Requirements to Maturity - It is the state's intention to retire substantially all notes payable at June 30, 1999 within one year. Debt Service requirements to maturity for all general obligation bonds payable at June 30, 1999 are as follows (expressed in thousands):

<u>For the Year(s)</u> <u>Ended June 30</u>	<u>General Obligation Bonds</u>		<u>Total</u> <u>Requirements</u>
	<u>Principal</u>	<u>Interest</u>	
2000	\$ 82,582	\$ 55,899	\$ 138,481
2001	80,337	51,256	131,593
2002	80,297	47,116	127,413
2003	74,457	43,006	117,463
2004	74,277	39,217	113,494
2005-2009	319,901	140,776	460,677
2010-2014	243,141	71,366	314,507
2015-2019	106,708	22,189	128,897
2020-2024	11,995	7,982	19,977
2025-2029	16,375	3,603	19,978
	<u>\$1,090,070</u>	<u>\$482,410</u>	<u>\$ 1,572,480</u>

D. Changes in General Long-Term Obligations - A summary of changes in general long-term obligations for the year ended June 30, 1999 follows (expressed in thousands).

	<u>Balance,</u> <u>July 1, 1998</u>	<u>General</u> <u>Obligation</u> <u>Debt</u> <u>Issued</u>	<u>General</u> <u>Obligation</u> <u>Debt</u> <u>Retired</u>	<u>Other Changes</u> <u>in General</u> <u>Long-Term</u> <u>Obligations</u>	<u>Balance,</u> <u>June 30, 1999</u>
General Obligation Bonds Payable	\$ 826,820	\$ 354,530	\$ (253,781)		\$ 927,569
General Obligation Notes Payable	92,850	97,656	(60,978)		129,528
Claims Payable	171,447			\$ (63,311)	108,136
Accrued Annual and Compensatory Leave	129,205			8,703	137,908
Lease Obligation Payable	588			(45)	543
<b>Total General Long Term Obligations</b>	<u>\$1,220,910</u>	<u>\$ 452,186</u>	<u>\$ (314,759)</u>	<u>\$ (54,653)</u>	<u>\$1,303,684</u>

The \$108.136 million above for Claims Payable represents the long-term obligation of \$59.644 million for Underground Storage Tanks, a Special Revenue Fund; \$16.643 million from Highway Fund, a Special Revenue Fund; and \$31.849 million payable from the General Fund.

Some \$6.186 million in bonds payable, \$48.764 million in refunding bonds and \$8.644 million in notes payable were issued to finance construction projects for facilities owned by the Facilities Revolving Fund, an Internal Service fund. These notes payable and bonds payable are reported as a liability of the Facilities Revolving Fund which is responsible for paying the debt service. These construction projects were managed by the Capital Projects Fund.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

E. General Obligation Bonds Authorized and Unissued - A summary of general obligation bonds authorized and unissued at June 30, 1999 is shown below (expressed in thousands). It is anticipated that a significant amount of these bonds will not be issued but will be canceled because of sufficient fund balances.

<u>Purpose</u>	<u>Unissued July 1, 1998</u>	<u>Authorized</u>	<u>Sold</u>	<u>Canceled</u>	<u>Unissued June 30, 1999</u>
Highway	\$ 736,300	\$ 83,800		\$ 94,800	\$ 725,300
Education	33,480		\$ 80	2,600	30,800
Environment and Conservation	63,258		13,951		49,307
General Government	655,439	53,926	147,424	30,745	531,196
Local Development Authority	27,000				27,000
Other	<u>500</u>	<u>225</u>	<u>225</u>		<u>500</u>
Totals	<u>\$ 1,515,977</u>	<u>\$ 137,951</u>	<u>\$ 161,680</u>	<u>\$ 128,145</u>	<u>\$ 1,364,103</u>

F. Capital Lease Obligations – The State leased a building for a vocational training center. The lease provides an option to purchase the building within the twelve-year lease period. Capital lease obligations are payable from resources of the General Fund. The property has been reported in the General Fixed Assets Account group as follows:

	<u>1999</u>
Land	\$ 56,000
Building	\$605,000

At June 30, 1999, minimum annual lease payments are as follows (expressed in thousands):

<u>For the Year(s) Ended June 30</u>	<u>Lease Obligation Payable</u>
2000	\$ 74
2001	74
2002	74
2003	74
2004	74
2005-2009	<u>314</u>
Total	684
<u>Less - Interest (5.1%)</u>	<u>141</u>
Present value of net minimum lease payments	<u>\$543</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

G. Component Units -Tennessee Housing Development Agency (THDA):

Bonds Payable and Notes at June 30, 1999, are shown below (expressed in thousands):

Revenue Bonds Payable - Tennessee Housing Development Agency mortgage finance program revenue bonds, various Series, 3.1% to 8.375%, due in amounts of principal and interest ranging from \$200.9 million in 2000 to \$3 million in 2031	\$1,640,100
Less: Unamortized bond refunding costs	<u>(5,242)</u>
Net Bonds Payable	<u>\$1,634,858</u>
THDA Single Family Mortgage Notes Trust Indenture, variable monthly interest rate, due April 2000	<u>\$ 65,235</u>

The revenue bonds and notes listed above are not obligations of the state. They are secured by pledge of resources from the facilities to which they relate and by certain other revenues, fees and assets of the Tennessee Housing Development Agency (THDA).

Debt service requirements to maturity for these revenue bonds payable at June 30, 1999, are as follows (expressed in thousands):

<u>For the Year(s)</u> <u>Ended June 30</u>	<u>Revenue Bonds</u>		<u>Total</u> <u>Requirements</u>
	<u>Principal</u>	<u>Interest</u>	
2000	\$ 112,246	\$ 88,691	\$ 200,937
2001	37,335	86,963	124,298
2002	40,790	85,128	125,918
2003	43,764	83,087	126,851
2004	44,909	80,901	125,810
2005-2009	265,566	392,642	658,208
2010-2014	256,492	312,129	568,621
2015-2019	297,411	228,812	526,223
2020-2024	320,397	107,989	428,386
2025-2029	187,078	23,001	210,079
2030-2031	11,659	412	12,071
	<u>\$1,617,647</u>	<u>\$1,489,755</u>	<u>\$ 3,107,402</u>

The above principal for revenue bonds is less than that presented on the accompanying financial statements by \$17.211 million. Of this amount, \$22.453 million represents accretion to date of interest on deep discount bonds in those years preceding the first principal payment on these bonds. This accretion has been reported above as interest in the years on which the bonds mature (2000-2017). In addition, \$5.242 million, which is a deduction from bonds payable for the deferred amount on refundings, is not reflected in the above presentation.

Bond sales during the year ended June 30, 1999 included the following issues:

- August 1998 - THDA program bonds of \$30 million.
- December 1998 - THDA program bonds of \$80 million.
- June 1999 - THDA program bonds of \$75 million.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

In August 1998, THDA issued \$30 million in Homeownership Program bonds of which \$27.15 million was used to refund previously issued bonds. The carrying amount of those bonds was \$26.897 million resulting in a difference between the reacquisition price and the net carrying amount of the old debt of \$253 thousand. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2027. The agency refunded the bonds to reduce its total debt service over the next 31 years by \$3,894,097 and realize an economic gain (the difference between the present value of the old and new debt service payments) of \$4,097,864. The agency also remarketed \$30 million in Homeownership Bonds; \$8.88 million in serial bonds and \$21.12 million in term bonds.

On December 2, 1998, THDA issued \$80 million in Homeownership Program bonds which was used to refund \$56.505 million in notes and \$6.38 million in bonds previously issued in the Mortgage Finance and Homeownership Program. The carrying amount of the bonds was \$6.341 million. A call premium of \$1.88 million was paid on the redemption. The refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$39,457. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2026 using the straight-line method. A portion of this refunding was accomplished using proceeds of short-term debt; therefore, the full economic impact was not determined at June 30, 1999.

The March 1999, THDA remarketed \$50 million in Homeownership Program bonds of which \$29.725 million was used to refund bonds. The agency completed the refunding to reduce its total debt over the next 28 years by \$12,161,239 and realized an economic gain (the difference between the present value of the old and new debt service payments) of \$7,484,437.

On June 17, 1999, THDA remarketed \$50 million in Homeownership Program Bonds. \$40.93 million was used to refund bonds outstanding in the Mortgage Finance Program and the Homeownership Program. The agency completed the refunding to reduce its total debt service over the next 31 years by \$4,800,345 and realize an economic gain of \$7,790,649. Also, on June 17, 1999, THDA issued \$75 million in Homeownership Program bonds. The issue will be used to refund \$60.205 million of notes and bonds.

THDA Bonds Payable were retired at par before maturity in the year ended June 30, 1999, in the Mortgage Finance Program Bonds in the amount of \$4.22 million and in the Homeownership Program Bonds in the amount of \$75.697 million. The carrying values of these bonds were \$4.18 million and \$75.044 million. This resulted in a loss to the Mortgage Finance Program of \$39 thousand and the Homeownership Program of \$661 thousand.

On July 1, 1998, the agency drew down \$17.245 million of the convertible notes, 1997 CN-1, to refund certain bonds previously issued in the Homeownership Program. The carrying amount of these bonds was \$17,081,062. The refunding resulted in a difference of \$163,938 between the reacquisition price and the net carrying amount of the old debt. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2022. Also, on this date, the agency used \$40.93 million of the proceeds from the Homeownership Program Bond Issue 1998-1 (remarketed on 6-4-98) to refund certain bonds previously issued in the Mortgage Finance Program and the Homeownership Program. The carrying amount of these bonds was \$40.6 million. The refunding resulted in a difference of \$327,284 between the reacquisition price and the net carrying amount of the old debt. This difference, reported in the accompanying financial statements as a deduction from bonds payable, is being charged to operations through the year 2026.

Under the bond resolutions, the Agency has the option to redeem bonds at an initial price of 103 percent and subsequently at prices declining to par. Generally, the redemption option cannot be exercised prior to the time the bonds have been outstanding for ten years. Certain special redemption options, as governed by the bond resolutions, are permitted prior to that time. The bonds are secured, as described in the applicable bond resolutions, by the revenues, monies, investments, mortgage loans, and other assets in the funds and accounts established by the resolutions.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

The Single Family Mortgage Notes Trust Indenture, dated December 1, 1997 (the "Trust Indenture"), provides for the issuance of Agency draw-down notes with a current maximum aggregate principal amount of \$65 million. On April 1, 1999, the Trust indenture was amended to provide for the maximum aggregate principal amount of \$200 million. The Notes bear interest, payable on the first Thursday of each succeeding month with respect to the principal amount drawn by the agency. The interest rate is equal to ninety percent (90%) of the bond equivalent yield as determined on the related rate date. On April 13, 1999, the initial principal amount of \$65.235 million was drawn to refund \$65.235 million in bonds previously issued in the Mortgage Finance Program and the Homeownership Program on July 1, 1999 (\$63.004 million early redemptions and \$2.231 million current maturities).

H. Component Units - Tennessee Local Development Authority (TLDA)

Bonds Payable and Notes Payable at June 30, 1999, are shown below (expressed in thousands):

Tennessee Local Development Authority revenue bonds, 4.75% to 7.25%, due in generally decreasing amounts of principal and interest from \$8 million in 2000 to \$16 thousand in 2022	\$64,523
Less: unamortized bond refunding costs	<u>(1,710)</u>
Net Bonds Payable	<u><u>62,813</u></u>
Tennessee Local Development Authority revenue bond anticipation notes, \$33.1 million at 3.5% due May 2000 and general obligation bond anticipation notes, \$16 million at variable rates due July 2002	\$49,100

The revenue bonds and revenue bond anticipation notes listed above are not obligations of the state. They are secured by pledge of resources from the facilities to which they relate and by certain other revenues, fees and assets of the Tennessee Local Development Authority (TLDA).

On June 2, 1999, the State Funding Board issued \$16.0 million of taxable general obligation notes for the Community Provider Program. Note proceeds combined with other funds available to the authority were used to advance refund \$11.515 million of series 1992 bonds and \$11.035 million of series 1994 bonds. The carrying amount of these bonds was \$22.55 million. The refunding resulted in a difference between the reacquisition price and the carrying amount of the old debt of \$2.012 million. The proceeds for the refunding were placed in an irrevocable trust; the bonds are considered to be defeased.

Debt Service requirements to maturity for TLDA's revenue bonds payable at June 30, 1999 are as follows (expressed in thousands):

<u>For the Year(s)</u> <u>Ended June 30</u>	<u>Revenue Bonds</u>		<u>Total</u> <u>Requirements</u>
	<u>Principal</u>	<u>Interest</u>	
2000	\$ 4,629	\$ 3,402	\$ 8,031
2001	3,784	3,173	6,957
2002	3,974	2,984	6,958
2003	4,174	2,783	6,957
2004	4,064	2,570	6,634
2005-2009	17,865	9,843	27,708
2010-2014	16,790	5,116	21,906
2015-2019	8,628	1,200	9,828
2020-2022	615	54	669
	<u>\$ 64,523</u>	<u>\$ 31,125</u>	<u>\$ 95,648</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

I. Component Units - Tennessee State School Bond Authority (TSSBA)

Bonds and Commercial Paper Payable at June 30, 1999 are shown below (expressed in thousands).

Tennessee State School Bond Authority revenue bonds, various Series, 3% to 6.7%, due in decreasing amounts of principal and interest from \$15.2 million in 2000 to \$3.5 million in 2028	\$ 174,401
Tennessee State School Bond Authority 1987 Refunding Revenue bonds, maturing in 2012	5,250
Tennessee State School Bond Authority 1989 Current Interest and College Savings Bonds, maturing to 2010	21,472
Tennessee State School Bond Authority 1990 Series A Taxable and Series B Tax Exempt Revenue Bonds, maturing to 2011	5,915
Tennessee State School Bond Authority 1996 Refunding Revenue Bonds, maturing to 2020	54,251
Tennessee State School Bond Authority 1998 Refunding Revenue Bonds, maturing to 2021	<u>73,014</u>
 Bonds Payable	 334,303
 Less: Unamortized bond refunding costs	 <u>(4,741)</u>
Net Bonds Payable	<u><u>329,562</u></u>
 Tennessee State School Bond commercial paper, variable rate	 <u><u>\$ 162,050</u></u>

The revenue bonds and commercial paper listed above are not obligations of the state. They are secured by pledge of resources from the facilities to which they relate and by certain other revenues, fees and assets of the Tennessee State School Bond Authority (TSSBA).

Debt Service requirements to maturity for TSSBA's revenue bonds payable at June 30, 1999 are as follows (expressed in thousands):

<u>For the Year(s)</u> <u>Ended June 30</u>	<u>Revenue Bonds</u>		<u>Total</u> <u>Requirements</u>
	<u>Principal</u>	<u>Interest</u>	
2000	\$ 18,004	\$ 17,466	\$ 35,470
2001	18,429	16,603	35,032
2002	18,530	15,879	34,409
2003	17,814	15,119	32,933
2004	18,850	14,367	33,217
2005-2009	74,557	61,089	135,646
2010-2014	61,515	36,596	98,111
2015-2019	40,155	22,051	62,206
2020-2024	35,574	11,629	47,203
2025-2028	20,768	2,484	23,252
	<u><u>\$324,196</u></u>	<u><u>\$213,283</u></u>	<u><u>\$ 537,479</u></u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

The above principal for revenue bonds is less than that presented on the accompanying financial statements by \$5.366 million. Of this amount, \$10.107 million represents accretion to date of interest on deep discount bonds in those years preceding the first principal payment on these bonds. This accretion has been reported above as interest in the years on which the bonds mature (2000-2010). In addition, \$4.741 million, which is a deduction from bonds payable for the deferred amount on refundings is not reflected in above presentation.

On October 1, 1998, the authority issued four series of bonds. 1998 Series A tax-exempt bonds in the amount of \$54.865 million was issued to redeem \$43.7 million of commercial paper and 1998 Series B taxable bonds in the amount of \$15.46 million to redeem \$2.2 million of commercial paper. The balance of the proceeds was used for new loans.

1998 Series C bonds were issued in the amount of \$48.735 million. In addition to the bond proceeds, a \$12,958,629 debt service reserve contribution, and taxable commercial paper proceeds in the amount of \$15 million were used to currently refund \$18.34 million of 1972 Series A bonds, \$1.78 million of 1977 Series A bonds, \$28.82 million of 1977 refunding bonds, and \$26.385 million of 1985 Series B bonds. The refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$847,146. Of this amount, \$274,486 is reported in the accompanying financial statements as an extraordinary loss. The remaining \$572,660 is reported as a deduction from bonds payable and is being charged to operations through the year 2014 using the straight-line method. The refunding was completed to reduce the authority's total debt service payments over the next 15 years by \$18.562 million and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$6.38 million.

1998 Series D bonds were issued in the amount of \$33.54 million. In addition to the bond proceeds, a \$4,378,018 debt service reserve contribution, and taxable commercial paper proceeds in the amount of \$6.8 million were used to advance refund \$40.775 million of 1992 Series A bonds. The monies were placed in an irrevocable trust and the bonds are considered to be defeased. The refunding resulted in a difference between the reacquisition price and the net carrying amount of the old debt of \$2,533,507. Of this amount, \$425,012 is reported in the accompanying financial statements as an extraordinary loss. The remaining \$2,108,495 is reported as a deduction from bonds payable and is being charged to operations through the year 2021 using the straight-line method. The refunding was completed to reduce the authority's total debt service payments over the next 22 years by \$11.203 million and to obtain an economic gain (difference between the present values of the old and new debt service payments) of \$2.548 million.

The authority issued taxable commercial paper in conjunction with these refundings to prepare for the conversion of the University of Tennessee Memorial Research Center and Hospital to a 501 (c) (3) corporation. Various hospital projects had been financed through the refunded bonds and the commercial paper was used to refund the bonds attributable to those projects.

On May 1, 1999, the authority liquidated \$3,957,600 of crossover refunding investments to call \$3.88 million of 1989 Current Interest Bonds. Call premiums of \$77,600 were paid on the refunding. The refunding resulted in a difference between the reacquisition price and the net carrying amount of the refunded debt of \$103 thousand, which is reported as a deduction from bonds payable and is being charged to operations through the year 2020 using the straight-line method.

Commercial Paper Program. The Tennessee State School Bond Authority issues short-term debt to finance certain capital projects for the State of Tennessee's higher education institutions. The Authority approved an increase in the maximum amount authorized from \$150 million to \$200 million on January 7, 1999. At the Program's inception, Commercial Paper refinanced certain outstanding bond anticipation note indebtedness that the Authority had previously issued to finance capital projects. The Commercial Paper dealer is J.P. Morgan & Co. At June 30, 1999, \$162.05 million of commercial paper was outstanding (\$96,600,000 of tax-exempt and \$65,450,000 of federally taxable Commercial paper).

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

The commercial paper is a special obligation of the Authority. Commercial paper principal and interest may be paid from: (i) the proceeds of draws on the Liquidity Facility, (ii) Available Revenues, (iii) the moneys and securities (if any) on deposit in the commercial paper and reimbursement account and in the Debt Service Fund, (iv) the moneys and securities (if any) on deposit in the Project Construction Account for such projects, and (v) the proceeds of bonds, notes or other evidences of indebtedness to the extent set aside to make such payments.

The maturity of the paper may not exceed 270 days and the maximum interest rate may not exceed 12%. Upon maturity, the paper is remarketed by the commercial paper dealer, redeemed, or extinguished with long-term debt. The Commercial Paper bears interest at a variable rate that is paid upon maturity. The higher education institutions contribute funds to the Interest Rate Reserve Fund. The principal of the Interest Rate Reserve Fund is credited back to the institution as Commercial Paper is redeemed. The Interest Rate Reserve Fund consisted of \$784,915 as of June 30, 1999.

The Commercial Paper liquidity provider, under an Advance Agreement, is *Westdeutsche Landesbank Girozentrale*, New York branch. The total available commitment is \$182.7 million. The obligation of *Westdeutsche Landesbank Girozentrale* is to purchase unremarketed Commercial Paper.

**NOTE 4 - INSURANCE RELATED ACTIVITIES**

- A. Teacher Group Insurance - The Teacher Group Insurance Fund, a public entity risk pool, was established in January 1986 to provide a program of health insurance coverage for the teachers of the political subdivisions of the state. In accordance with Tennessee Code Annotated 8-27-302 all local education agencies are eligible to participate. Fund members at June 30, 1999, included 117 local education agencies and two education cooperatives, with 35,942 teachers and support personnel, and 1,902 retirees enrolled in one of three health care options: preferred provider plan, point of service plan, or a health maintenance organization. The state does not retain any risk for losses by this fund.

The Teacher Group Insurance Fund assumes responsibility for: determining plan benefits and eligibility, establishing premiums sufficient to fund plan obligations, recording and reporting financial transactions accurately, reporting enrollment to vendors, processing of claims submitted for services provided to plan participants, communicating with plan participants, and complying with appropriate state and federal law and regulation. Plan participants are required to: pay premium on time, file claims for services received, report changes in eligibility of themselves or their dependents, and insure that only eligible expenses are paid by the plan. Individuals who cancel coverage may be required to demonstrate a qualifying event to rejoin the plan. Employers must wait twenty-four months before rejoining the plan should the employer elect to withdraw from the plan. In the case of individuals or groups rejoining the plan, a preexisting condition exclusion currently applies.

The Teacher Group Insurance Fund establishes claims liabilities for self-insured options based on estimates of the ultimate cost of claims that have been reported but not settled, and of claims that have been incurred but not reported. Teachers and providers have 13 months to file medical claims. The process used to compute claims liabilities does not necessarily result in an exact amount. Claims liabilities are recomputed periodically using actuarial and statistical techniques to produce current estimates, which are 16.5% of the prior 12 months claims. Adjustments to claims liabilities are charged or credited to expense in the period in which they are made. The Teacher Group Insurance Fund considers investment income in determining if a premium deficiency exists.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

As discussed above, the Teacher Group Insurance Fund establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities during the past two years (expressed in thousands):

	<u>1999</u>	<u>1998</u>
Unpaid Claims at Beginning of Year	\$ 13,263	\$15,017
Incurred Claims, Provision for Insured Events of the Current Year	<u>93,546</u>	<u>79,297</u>
Total Incurred Claims Expenses	106,809	94,314
Payments	<u>91,716</u>	<u>81,051</u>
Total Unpaid Claims at End of the Year	<u>\$ 15,093</u>	<u>\$ 13,263</u>

- B. Local Government Group Insurance - The Local Government Group Insurance Fund, a public entity risk pool, was established in July 1991 to provide a program of health insurance coverage for employees of local governments and quasi-governmental organizations that were established for the primary purpose of providing services for or on the behalf of state and local governments. In accordance with Tennessee Code Annotated 8-27-207 all local governments and quasi-governmental organizations described above are eligible to participate. Fund members at June 30, 1999, included 29 counties, 74 municipalities and 149 quasi-governmental organizations, with 11,976 employees and 363 retirees maintaining coverage through one of three options: preferred provider plan, point of service plan, or a health maintenance organization. The state does not retain any risk for losses by this fund.

The Local Government Group Insurance Fund assumes responsibility for: determining plan benefits and eligibility, establishing premiums sufficient to fund plan obligations, recording and reporting financial transactions accurately, reporting enrollment to vendors, the processing of claims submitted for services provided to plan participants, communicating with plan participants, and complying with appropriate state and federal law and regulation. Plan participants are required to: pay premium on time, file claims for services received, report changes in eligibility of themselves or their dependents, and insure that only eligible expenses are paid by the plan. Individuals who cancel coverage may be required to demonstrate a qualifying event to rejoin the plan. Employers must wait twenty-four months before rejoining the plan should the employer elect to withdraw from the plan. In the case of individuals or groups rejoining the plan, a preexisting condition exclusion currently applies.

The Local Government Group Insurance Fund establishes claims liabilities for self-insured options based on estimates of the ultimate cost of claims that have been reported but not settled, and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims. The process used to compute claims liabilities does not necessarily result in an exact amount. Claims liabilities are recomputed periodically using actuarial and statistical techniques to produce current estimates, which are 16% of the prior 12 months claims. Adjustments to claims liabilities are charged or credited to expense in the period in which they are made. The Local Government Group Insurance Fund considers investment income in determining if a premium deficiency exists.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

As discussed above, the Local Government Group Insurance Fund establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities during the past two years (expressed in thousands):

	<u>1999</u>	<u>1998</u>
Unpaid Claims at Beginning of Year	\$ 3,232	\$ 4,251
Incurred Claims, Provision for Insured Events of the Current Year	<u>20,244</u>	<u>19,499</u>
Total Incurred Claims Expenses	23,476	23,750
Payments	<u>20,245</u>	<u>20,518</u>
Total Unpaid Claims at End of the Year	<u>\$ 3,231</u>	<u>\$ 3,232</u>

- C. Risk Management - It is the policy of the state not to purchase commercial insurance for the risks of losses for general liability, automobile liability, professional malpractice and workers' compensation. The state management believes it is more economical to manage its risks internally and set aside assets for claim settlement in its internal service fund, the Claims Award Fund (CAF). CAF services claims for risk of loss to which the state is exposed, including general liability, automobile liability, professional malpractice, and workers' compensation. All agencies and authorities of the state participate in CAF, except for the Supreme Court Boards, The Dairy Promotion Board, TN 200 (a component unit), and Certified Cotton Grower's Organization (a component unit). CAF allocates the cost of providing claims servicing and claims payment by charging a premium to each agency based on a percentage of each organization's expected loss costs which include both experience and exposures. This charge considers recent trends in actual claims experience of the state as a whole. An actuarial valuation is performed as of each fiscal year end to determine the fund liability and premium allocation.

CAF liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Liabilities include an amount for claims that have been incurred but not reported. Because actual claims liabilities depend on such complex factors as inflation, changes in legal doctrines, and damage awards, the process does not result in an exact amount. Claims liabilities are reevaluated annually to take into consideration recently settled claims, the frequency of claims, and other economic and social factors. At June 30, 1999 the amount of these liabilities was \$61.561 million, which are discounted at 5.35%. Changes in the balances of claims liabilities during fiscal years 1998 and 1999 were as follows (expressed in thousands):

	Beginning of Fiscal Year <u>Liability</u>	Current Year Claims and <u>Changes in Estimates</u>	Claim <u>Payments</u>	Balance at Fiscal <u>Year-End</u>
1997-98	\$ 53,462	\$ 21,645	\$ (19,443)	\$ 55,664
1998-99	\$ 55,664	\$ 24,941	\$ (19,044)	\$ 61,561

At June 30, 1999, CAF held \$72.3 million in cash and cash equivalents designated for payment of these claims.

The state purchases commercial insurance for real property losses above \$5 million per year and surety bond coverage on the state's officials and employees. During FY 99, the state incurred losses in Clarksville and Jackson due to damage from tornadoes. Final settlement has not been made but is expected to be approximately \$6 million. In the prior two fiscal years the state had not had any claims filed with the commercial insurer. A designation for casualty losses in the amount of \$8.219 million has been established in the General Fund to provide for any property losses other than the commercial insurance coverage.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

- D. Employee Group Insurance - The Employee Group Insurance Fund, an entity other than a pool, was established in 1979 to provide a program of health insurance coverage for the employees of the state with the risk retained by the state, therefore it is accounted for as an Internal Service Fund. In accordance with Tennessee Code Annotated 8-27-201 all state employees, retirees, and former employees with work related injuries are eligible to participate. Fund members at June 30, 1999, included 64,166 employees and 5,149 retirees enrolled in one of three options: preferred provider plan, point of service plan, or Health Maintenance Organization.

The Employee Group Insurance Fund establishes claims liabilities for self-insured options based on estimates of the ultimate cost of claims that have been reported but not settled, and of claims that have been incurred but not reported. Employees and providers have 13 months to file medical claims. The process used to compute claims liabilities does not necessarily result in an exact amount. Claims liabilities are recomputed periodically using actuarial and statistical techniques to produce current estimates, which are 17% of the prior 12 months claims. Adjustments to claims liabilities are charged or credited to expense in the period in which they are made. The Employee Group Insurance Fund considers investment income in determining if a premium deficiency exists.

As discussed above, the Employee Group Insurance Fund establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities during the past two years (expressed in thousands):

	<u>1999</u>	<u>1998</u>
Unpaid Claims at Beginning of Year	\$ 33,133	\$ 33,243
Incurred Claims, Provision for Insured Events of the Current Year	<u>200,710</u>	<u>188,288</u>
Total Incurred Claims Expenses	233,843	221,531
Payments	<u>200,161</u>	<u>188,398</u>
Total Unpaid Claims at End of the Year	<u>\$ 33,682</u>	<u>\$ 33,133</u>

**NOTE 5 - PENSION PLANS**

- A. State Defined Benefit Plan - The State of Tennessee contributes to the State Employees, Teachers, and Higher Education Employees Pension Plan (SETHEEPP), a cost-sharing multiple employer defined benefit pension plan administered by the Tennessee Consolidated Retirement System (TCRS) and consisting of 142 participating employers. The TCRS provides retirement benefits as well as death and disability benefits to plan members and their beneficiaries. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members who are at least 55 years of age or have 25 years of service. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the plan on or after July 1, 1979 are vested after five years of service. Members joining prior to July 1, 1979 are vested after four years of service. Benefit provisions are established by state statute found in Title 8, Chapters 34-37 of the Tennessee Code Annotated (TCA). State statutes are amended by the Tennessee General Assembly. Cost of living adjustments (COLA) are provided each July based on the percentage change in the Consumer Price Index (CPI) during the previous calendar year. No COLA is granted if the CPI increases less than one-half percent; a COLA of one percent will be granted if the CPI increases between one-half percent and one percent; the maximum annual COLA is capped at three percent.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for SETHEEPP. That report may be obtained by writing to the Tennessee Treasury Department, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, TN 37243-0230 or by calling (615) 741-7063.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

Plan members are noncontributory. The State of Tennessee is required to contribute at an actuarially determined rate. The current rate is 3.65% of annual covered payroll. The contribution requirements of the State of Tennessee are established and may be amended by the TCRS Board of Trustees. The State's contributions to TCRS for the years ending June 30, 1999, 1998, and 1997 were \$244.453 million, \$166.756 million and \$278.417 million respectively, equal to the required contributions for each year.

- B. Political Subdivision Defined Benefits Plan - TCRS administers the Political Subdivision Pension Plan (PSPP), which is an agent multiple-employer defined benefit pension plan that covers employees of 365 participating political subdivisions. The PSPP provides retirement benefits as well as death and disability benefits to plan members and their beneficiaries. Benefits are determined by a formula using the member's high five-year average salary and years of service. Members become eligible to retire at the age of 60 with five years of service or at any age with 30 years of service. A reduced retirement benefit is available to vested members who are at least 55 years of age or have 25 years of service. Disability benefits are available to active members with five years of service who become disabled and cannot engage in gainful employment. There is no service requirement for disability that is the result of an accident or injury occurring while the member was in the performance of duty. Members joining the plan prior to July 1, 1979 are vested after four years of service. Members joining on or after July 1, 1979 are vested upon completion of 10 years of service, unless five years vesting is authorized by resolution of the chief governing body. Benefit provisions are established and amended by state statute. Cost of living adjustments, if adopted by a political subdivision, are provided each July based on the percentage change in the Consumer Price Index (CPI) during the previous calendar year. No COLA is granted if the CPI increases less than one-half percent; a COLA of one percent will be granted if the CPI increases between one-half percent and one percent; the maximum annual COLA is capped at three percent. Pursuant to Article Two, Section 24 of the Constitution of the State of Tennessee, the state cannot mandate costs on local governments. Any benefit improvement may be adopted by the governing body of a governmental entity participating in the TCRS.

The TCRS issues a publicly available financial report that includes financial statements and required supplementary information for PSPP. The PSPP report may be obtained by writing to the Tennessee Treasury Department, Consolidated Retirement System, 10th Floor Andrew Jackson Building, Nashville, TN 37243-0230 or by calling (615) 741-7063.

- C. Defined Contribution Plan - The Optional Retirement Plan (ORP) as administered by the Tennessee Treasury Department is a defined contribution plan. The ORP was established by state statute in Title 8, Chapter 35, Part 4 of the TCA. This statute also sets out the plan provisions. State statutes are amended by the Tennessee General Assembly. The ORP was designed to provide benefits at retirement to faculty and staff of the Tennessee Board of Regents institutions and the University of Tennessee system who are exempt from the overtime provision of the Fair Labor Standards Act and who waive membership in the TCRS. In a defined contribution plan, benefits depend solely on amounts contributed to the plan plus investment earnings. Plan members are noncontributory. The State of Tennessee contributes 10% of the employee's base salary up to the social security wage base and 11% above the social security wage base. Members are fully vested upon entry into the plan. The required contributions made by the State of Tennessee to the ORP were \$55.6 million for the year ending June 30, 1999.
- D. Deferred Compensation - The state offers its employees two deferred compensation plans, one established pursuant to IRC Section 457 and the other pursuant to IRC Section 401 (k). All costs of administering and funding these programs are the responsibility of plan participants.

The Section 401(k) and Section 457 plan assets remain the property of the contributing employees, they are not presented in the accompanying financial statements. IRC Sections 401(k) and 457 establishes participation, contribution and withdrawal provisions for the plans. During the year ended June 30, 1999, contributions totaling \$50.4 million were made by employees participating in the plans. Another \$5.02 million was contributed by the State as matching contributions up to \$20 per employee per month for the 401(k) plan match.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

**NOTE 6 - POST EMPLOYMENT HEALTH INSURANCE BENEFITS**

- A. General - The state offers an opportunity to its employees and eligible retirees to participate in a self-insured indemnity policy, a point of service plan, or health maintenance organizations. This post employment benefit is authorized under Tennessee Code Annotated 8-27-205. The indemnity policy (preferred provider plan) provides benefits to plan participants in a comprehensive, major medical format involving a \$200 calendar year deductible and a \$1,000 per individual out-of-pocket limit. The plan incorporates typical provisions relating to utilization review, medical necessity, pre-existing conditions, coordination of benefits and subrogation of expenses. The plan offers benefit incentives for the use of designated providers and the plan maintains limitations on benefits provided for the treatment of mental illness and substance abuse.
- B. Retirees - Retirees who are not yet eligible for Medicare benefits may continue participation in the plan subject to certain length of service and participation requirements. Upon Medicare eligibility, the retiree is afforded the opportunity to participate in a fully-insured supplement policy not associated with the plan. The state pays a service determined amount for retirees who participate in the state sponsored Medicare supplement policy.

The funds collected for the plan's operation are recorded in the employee group insurance account. The plan's premiums are intended to fund benefits on a pay-as-you-go basis and no specified reserves have been established to fund retiree health benefits. Current retiree premium rates are based upon the retiree's length of service and range from 20 percent to 40 percent of the plan's total premium. The state provides no direct funding of retiree health benefits.

During the 1998-99 fiscal year, the Preferred Provider Plan provided approximately \$22.5 million in benefits to an average of 4,332 retired employee participants.

- C. Cobra - Federal law requires large employers to continue health insurance benefits to employees who have terminated employment for up to 18 months. The former employees must pay 102 percent of the total premium (employee plus employer share), funded on a pay as you go basis. Insurance coverage is not mandatory if the former employee is eligible for Medicare or has coverage with another group medical plan. The state covered an average of 310 former employees during fiscal year 1998-99, and the Preferred Provider Plan paid approximately \$1.5 million in benefits to this group.

**NOTE 7 - INVESTMENT POOL**

The State Pooled Investment Fund (SPIF) is an external investment pool sponsored by the State of Tennessee. The external portion of SPIF is the Local Government Investment Pool (LGIP) and is reported as a separate investment trust fund. The internal portion, consisting of funds belonging to the state and its component units, has been included in the various funds and component units.

A copy of the SPIF report can be obtained by writing Tennessee Treasury Department, Accounting Division, 9<sup>th</sup> Floor Andrew Jackson Building, Nashville, TN 37243-0231 or by calling (615) 741-1337.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

**NOTE 8 - DEPOSITS AND INVESTMENTS**

- A. Investment Policy - The Pooled Investment Fund, administered by the State Treasurer, is authorized by statute to invest funds in accordance with policy guidelines approved by the State Funding Board. The current resolution of that Board gives the Treasurer approval to invest in collateralized certificates of deposit in authorized state depositories; prime commercial paper and prime banker's acceptances; bonds, notes and bills of the United States Treasury or other obligations guaranteed as to principal and interest by the United States or any of its agencies and in repurchase agreements for obligations of the United States or its agencies which are fully guaranteed as to principal and interest by the United States; mutual funds which are limited to investments of the above permitted kinds; and in certain obligations of the state. This resolution further states that the dollar weighted average maturity of the State Pooled Investment Fund shall not exceed 90 days and that no investment may be purchased with a remaining maturity of greater than 397 calendar days. Provided however, an amount not to exceed the lesser of \$300 million or twenty percent (20%) of the book value of the State Pooled Investment Fund at the time such investments are made, may be invested in maturities greater than one year but not greater than five years. The State Pooled Investment Fund is also authorized by policy to contractually loan securities to investment brokers. On January 17, 1995, the State terminated the securities lending contract and therefore had no securities on loan from the State Pooled Investment Fund. Statutes require the state deposits be secured by collateral securities with a market value of 105% of the face of the deposit secured thereby after considering the applicable FDIC coverage, or the depository must be a member of the State Collateral Pool and the pool must have securities pledged which in total equal the required percentage established by the Collateral Pool Board. In addition, statutes require that financial institutions with a capital-to-assets ratio of less than five percent (5%) must pledge an additional \$100 thousand of collateral securities.

Certificates of deposit are not placed or renewed with a financial institution until adequate collateral is pledged. Open accounts maintained for deposit of state revenues are collateralized on an estimate of the average daily balance in the account based on previous balances and monitored for variation to actual balances. The Treasurer is required, by statute, to evaluate the market value of required collateral monthly, and more frequently if market conditions require. Further, statutes provide the Commissioner of Financial Institutions to advise, on a timely basis, the Treasurer and the Commissioner of Finance and Administration of the condition of each state bank and state chartered savings and loan association, including his recommendations regarding its condition and safety as a state depository. Similar provisions apply to federally chartered banks and savings and loan associations designated as state depositories. This process ensures that institutions whose financial status is uncertain are monitored for collateral sufficiency. All repurchases are done with primary dealers in government securities which have executed a master repurchase agreement with the State which provides for securities underlying repurchase agreements to have a market value of not less than 100 percent nor more than 102 percent of the cost of the repurchase agreement plus accrued interest. Prime commercial paper may be acquired from authorized broker dealers or directly from the issuer. There is no collateral requirement for prime commercial paper.

The Tennessee Consolidated Retirement System (TCRS), in addition to the guidelines outlined for the Pooled Investment Fund, may invest in long-term investments. The TCRS may invest in bonds, debentures, preferred stock and common stock, and other good and solvent securities subject to the TCRS Board of Trustees approval. The Board has also authorized limited investments of securities in some foreign countries. TCRS may also invest in multifamily residential real estate through direct equity investment vehicles including, but not limited to, sole proprietorship and joint ventures.

B. Valuation of Investments

1. State Pooled Investment Fund – The SPIF is not registered with the Securities and Exchange Commission (SEC) as an investment company but, through its investment policy adopted by the Funding Board of the State of Tennessee (Funding Board), operates in a manner consistent with the SEC's rule 2a7 of the Investment Company Act of 1940. Rule 2a7 allows SEC registered mutual funds to use amortized cost to report net assets in computing share prices. Likewise, the SPIF uses amortized cost accounting measures to report investments and share prices. During the fiscal year ended June 30, 1999, the State had not obtained or provided any legally binding guarantees to support the value of participant shares.
2. Other Investments – Investments not included in the SPIF are valued at fair value or amortized cost.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

- C. Securities Lending - The TCRS and the Chairs of Excellence (COE), a non-expendable trust fund, are authorized by their investment policies, as adopted by their boards, to enter into collateralized securities lending agreements whereby the TCRS and COE loans its debt and equity securities for a fee to a select few of the highest quality securities firms and banks. Loans must be limited so the total amount on loan does not exceed 30 percent of the TCRS' and COE's assets. The TCRS' and COE's custodian bank manages the lending program and maintains the collateral on behalf of the TCRS and COE. The borrower may deliver collateral to the lending agent in the form of cash or bonds, notes, and treasury bills of the United States or other obligations guaranteed as to principal and interest by the United States or any of its agencies or by the Federal Home Loan Mortgage Corporation, Federal National Mortgage Association, Student Loan Marketing Association and other United States government sponsored corporations or enterprises. Cash received as collateral may be reinvested by the lending agency in accordance with the investment policy, as further restricted under the TCRS and COE securities lending agreement. Collateral securities cannot be pledged or sold unless the borrower defaults.

The loaned securities are initially collateralized at 102 percent of their fair value for domestic securities and 105 percent for international. Collateral is marked-to-market daily and additional collateral is pledged by the borrower if the fair value of the collateral subsequently falls below 100 percent for domestic securities and 105 percent for international. Although there is no specific policy for matching the maturities of the collateral investments and the securities loans, all securities on loan can be terminated on demand by either the TCRS/COE or the borrower. At year-end, TCRS and COE had no securities on loan.

- D. Deposits - Deposits with financial institutions are required to be categorized to indicate the level of risk assumed by the state. Category 1 consists of deposits that are insured or collateralized with securities held by the state or by its agent in the state's name. Category 2 consists of deposits collateralized with securities held by the pledging financial institution's trust department or agent in the state's name. Category 3 deposits are uncollateralized. This includes any bank balance that is collateralized with securities held by the pledging financial institution, or by its trust department or agent but not in the state's name.

At year end, the carrying amount of deposits in all funds was \$1,767.052 million and the bank balance, including accrued interest, was \$1,796.455 million. Of the bank balance, \$1,796.276 million was (category 1) covered by insurance or collateral (valued at market) held in the state's name by independent custodial banks or segregated in the Federal Reserve Bank in the state's account and \$179 thousand was (category 3) uninsured and uncollateralized.

Cash on deposit with fiscal agent includes \$9.302 million of cash held in a custody account by State Street Bank under a contractual arrangement for master custody services. Monies with the custodial agent are not classified by credit risk, as the custody account relationship does not meet the definition for either a deposit with a financial institution or a security.

- E. Investments - Investments are also required to be categorized to indicate the level of risk assumed by the state. Category 1 consists of investments that are insured or registered or for which the securities are held by the state or its agent in the state's name. Category 2 consists of uninsured and unregistered investments for which the securities are held by the counterparties' trust department or agent in the state's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparties' trust department or agent but not in the state's name. Investments are categorized below for all funds (expressed in thousands):

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

PENSION TRUST, POOLED INVESTMENT, AND OTHER FUNDS

	Category			Carrying Amount	Fair Value 6/30/99
	1	2	3		
Cash Equivalents and Short-Term Investments:					
Commercial Paper	\$ 1,518,428			\$ 1,518,428	\$ 1,518,428
Repurchase Agreements	214,000			214,000	214,000
Government Securities	<u>974,908</u>			<u>974,908</u>	<u>974,290</u>
Total Cash Equivalents and Short-Term Investments	<u>2,707,336</u>			<u>2,707,336</u>	<u>2,706,718</u>
Long-Term Investments:					
Domestic Securities:					
Government Securities - not on loan	8,171,682			8,171,682	8,171,682
Corporate Bonds	2,960,904			2,960,904	2,960,904
Corporate Stocks	7,337,502			7,337,502	7,337,502
Margin Deposits on Future Contracts:					
Domestic Government Bonds			\$ 11,319	11,319	11,319
International Securities:					
Government Bonds	1,016,111			1,016,111	1,016,111
Corporate Bonds	442,771			442,771	442,771
Corporate Stocks	<u>2,113,389</u>			<u>2,113,389</u>	<u>2,113,389</u>
Total Long-Term Investments	<u>22,042,359</u>		<u>11,319</u>	<u>22,053,678</u>	<u>22,053,678</u>
	<u>\$24,749,695</u>		<u>\$ 11,319</u>	24,761,014	24,761,014
Domestic Securities:					
Mutual Funds				4,058	4,058
Unsettled Investment Acquisitions:					
Domestic Securities:					
Government Bonds				155,578	155,578
Corporate Bonds				52,752	52,752
Corporate Stocks				17,307	17,307
International Securities:					
Corporate Stocks				11,080	11,080
Unemployment Compensation Pool				<u>896,589</u>	<u>896,589</u>
Total Investments and Cash Equivalents				<u>\$25,898,378</u>	<u>\$25,898,378</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

F. Component Units

The various component units are generally governed by the same basic State statutes as the State's investments described in Note 8A.

1. University of Tennessee

At year end, the carrying amount of deposits for the University of Tennessee was \$12.231 million and the bank balance was \$13.384 million. The entire bank balance was (category 1) covered by insurance or collateral (valued at market) held in the University's name by independent custodial banks.

The investments for the University of Tennessee are categorized below (expressed in thousands):

	Category			Carrying Amount	Fair Value 6/30/99
	1	2	3		
Cash Equivalents:					
Commercial Paper	\$ 109,177			\$ 109,177	\$ 109,177
Repurchase Agreements	21,000			21,000	21,000
Government Securities	<u>198,059</u>			<u>198,059</u>	<u>198,059</u>
Total Cash Equivalents	<u>328,236</u>			<u>328,236</u>	<u>328,236</u>
Investments:					
Domestic Securities:					
Government Securities	15,624	\$ 38,675		54,299	54,299
Corporate Bonds	3,013	30,711		33,724	33,724
Corporate Stocks	123,683	8,314		131,997	131,997
Collateralized Mortgage Securities	2,445			2,445	2,445
Assets with Counter-Party			\$ 13,618	13,618	13,618
Other	195			195	195
International Securities:					
Corporate Stocks	<u>2,584</u>			<u>2,584</u>	<u>2,584</u>
Total Investments	<u>147,544</u>	<u>77,700</u>	<u>13,618</u>	<u>238,862</u>	<u>238,862</u>
	<u>\$ 475,780</u>	<u>\$ 77,700</u>	<u>\$ 13,618</u>	<u>567,098</u>	<u>567,098</u>
Limited Partnership-Venture					
Capital Funds				21,812	21,812
Real Estate Equity				17,977	17,977
Mutual Funds				155,393	155,393
Real Estate Gifts				7,006	7,006
Cash Equivalents - assets with bank as custodian				<u>4,878</u>	<u>4,878</u>
Total Investments and Cash Equivalents				<u>\$ 774,164</u>	<u>\$ 774,164</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

2. Tennessee Board of Regents -

At year end, the carrying amount of deposits for the Tennessee Board of Regents was \$36.319 million and the bank balance was \$60.673 million. Of the bank balance, \$57.846 million was (category 1) covered by insurance or collateral (valued at market) held in the University's name by independent custodial banks or segregated in the Federal Reserve Bank in the University's name, \$236 thousand was (category 2) collateralized with securities held by the pledging financial institution's trust department or agent in the University's name, and \$2.591 million was (category 3) uninsured and uncollateralized. In addition, at June 30, 1999, the University had \$216.396 million being held by the State in the Local Government Investment Pool.

The investments for the Tennessee Board of Regents are categorized below (expressed in thousands):

	Category			Carrying Amount	Fair Value 6/30/99
	1	2	3		
Investments:					
Domestic Securities:					
Commercial Paper	\$ 4,943			\$ 4,943	\$ 4,943
Government Securities	46,139	\$ 3,815	\$ 2,956	52,910	52,910
Corporate Bonds	2,242	4,443	910	7,595	7,595
Corporate Stocks	8,188	8,884	1,776	18,848	18,848
Other	8,715			8,715	8,715
Total Investments	\$ 70,227	\$ 17,142	\$ 5,642	\$ 93,011	\$ 93,011
Mutual Funds				15,208	15,208
				\$ 108,219	\$ 108,219
Total Investments and Cash Equivalents				\$ 108,219	\$ 108,219

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

3. Tennessee Housing Development Agency

At year end, the carrying amount of deposits was \$22.219 million for the Tennessee Housing Development Agency (THDA). THDA's deposits are in financial institutions which participate in the bank collateral pool administered by the State Treasurer. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of custodial credit risk disclosure. In addition, at June 30, 1999, THDA had \$53.930 million being held by the State in the State Pooled Investment Fund.

The investments for the Tennessee Housing Development Agency are categorized below (expressed in thousands):

	Category			Carrying Amount	Fair Value 6/30/99
	1	2	3		
Cash Equivalents and Short-Term Investments:					
Repurchase Agreements	\$ 156,275			\$ 156,275	\$ 156,275
Government Securities	<u>174,063</u>			<u>174,063</u>	<u>174,063</u>
Total Cash Equivalents and Short-Term Investments	<u>330,338</u>			<u>330,338</u>	<u>330,338</u>
Long-Term Investments					
Government Securities	<u>432,160</u>			<u>432,160</u>	<u>432,160</u>
Long-Term Investments	<u>432,160</u>			<u>432,160</u>	<u>432,160</u>
Total Investments and Cash Equivalents	<u>\$ 762,498</u>			<u>\$ 762,498</u>	<u>\$ 762,498</u>

4. Tennessee State School Bond Authority

At year end, the carrying amount of deposits was \$137 thousand for the Tennessee State School Bond Authority (TSSBA). TSSBA's deposits are in financial institutions which participate in the bank collateral pool administered by the State Treasurer. The securities pledged to protect these accounts are pledged in the aggregate rather than against each individual account. The members of the pool may be required by agreement to pay an assessment to cover any deficiency. Under this additional assessment agreement, public fund accounts covered by the pool are considered to be insured for purposes of custodial credit risk disclosure. In addition, at June 30, 1999, TSSBA had \$24.067 million being held by the State in the State Pooled Investment Fund.

The investments for the Tennessee School Bond Authority are categorized below (expressed in thousands):

	Category			Carrying Amount	Fair Value 6/30/99
	1	2	3		
Investments:					
Domestic Securities:					
Government Securities	<u>\$ 26,159</u>			<u>\$ 26,159</u>	<u>\$ 26,159</u>
Total Investments	<u>\$ 26,159</u>			<u>\$ 26,159</u>	<u>\$ 26,159</u>

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

**NOTE 9 - COMMITMENTS AND CONTINGENCIES**

- A. Sick Leave - It is the state's policy to record the cost of sick leave when paid. Generally, since sick leave (earned one day per month with unlimited accumulation) is paid only when an employee dies or is absent due to illness, injury or related family death, there was no liability for sick leave at June 30, 1999. The estimated accumulated amount of unused sick leave at that date was \$321 million.
- B. Operating Leases - The state has entered into various operating leases for land, buildings and equipment. All leases contain termination clauses providing for cancellation after 30, 60 or 90 days' written notice to lessors. In addition, all leases contain appropriation clauses indicating that continuation of the lease is subject to funding by the legislature. It is expected that in the normal course of business most of these leases will be replaced by similar leases. Facilities Revolving Fund, an Internal Service Fund, has entered into various operating leases which have noncancelable lease terms. Below is a schedule of future minimum lease payments under these leases (expressed in thousands).

<u>For the Year(s)</u> <u>Ended June 30</u>	<u>Noncancelable</u> <u>Operating Leases</u>
2000	\$ 8,761
2001	5,788
2002	4,560
2003	3,216
2004	1,748
later years	<u>2,343</u>
Total Minimum Payments Required	<u>\$ 26,416</u>

Expenditures for rent under leases for the years ended June 30, 1999 and 1998 amounted to \$32.6 million and \$28.8 million, respectively.

- C. Highway Construction Projects - At June 30, 1999, the Department of Transportation had contractual commitments of approximately \$444.5 million for construction of various highway projects. Funding of these future expenditures is expected to be provided from federal grants (\$350.9 million) and general obligation bond proceeds (\$93.6 million).
- D. Litigation - Litigation has been brought against the State which challenges the conditions at Arlington Developmental Center. The State is under court order to remedy the situation and believes the Center is making satisfactory progress. In addition, the State was involved in litigation involving the Clover Bottom Developmental Center. A settlement was reached in the Clover Bottom litigation under which the State would work toward community placement of persons with developmental disabilities from all three developmental centers.

The small school systems in the state have previously filed suit against the state challenging the constitutionality of the funding formula for elementary and secondary education. The state Supreme Court held that the formula did violate the constitution. In response, the General Assembly enacted the Teachers Salary Equity Plan. A motion has been filed by the plaintiffs which asserts that the state has failed to equalize teacher salaries.

The State is also party to numerous other legal proceedings, many of which normally recur in governmental operations. In the opinions of the Attorney General and General Counsel for the University of Tennessee system, final settlement of these matters will have no material effect on the accompanying financial statements.

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

- E. Federal Grants - The state receives significant financial assistance from the federal government in the form of grants and entitlements. The receipt of federal grants is generally conditioned upon compliance with terms and conditions of the grant agreements and applicable federal regulations. Substantially, all federal grants are subject to either federal single audits or financial and compliance audits by grantor agencies or their representatives. Questioned costs as a result of these audits may become disallowances after the appropriate review of federal agencies. Material disallowances are recognized as either fund liabilities or liabilities of the General Long-Term Obligations Account Group when the loss becomes probable and reasonably estimable.

The Health Care Financing Administration (HCFA) has performed a review of the provider taxes collected for the period beginning fiscal year 1992 to the present. The purpose of the review was to determine the correlation between nursing home provider taxes and a state grant program for private pay patients of nursing homes (Grant Assistance Program). The resulting draft-report has not been received by the State of Tennessee for review and comments.

Other audits of the Medical Assistance Program (TennCare) have resulted in significant amounts of known and likely questioned costs that could be determined to be disallowances by the U.S. Department of Health and Human Services (HHS). These questioned costs relate to expenditure of resources for ineligible TennCare enrollees and for unauthorized services. The ultimate liability to the federal government, if any, cannot presently be determined. If HHS were to impose a liability, the state would appeal the decision.

Inconsistencies in the rate setting process for residential treatment services provided to children in state custody may have created over-billings to the TennCare Program. Any potential overpayment by HHS because of these inconsistencies cannot be quantified.

- F. Loan Guarantees - The Tennessee Student Assistance Corporation (TSAC), a component unit, operates the Guaranteed Student Loans Program. The U. S. Department of Education (USDE) reinsures the student loans up to 100% of their principal amounts. At June 30, 1999, TSAC was guarantor of \$1.983 billion in student loans, substantially all of which were reinsured by the USDE. The state has no obligation under these student loan guarantees in the event of default.
- G. Nashville Correctional Facilities Revenue Bonds - In June 1991, revenue bonds were issued by the Metropolitan Government of Nashville which have an outstanding balance of some \$19.7 million as of June 30, 1999. These bonds are obligations of the Metropolitan Government of Nashville. The state is committed to pay Nashville for the housing of locally sentenced inmates, including debt service on the bonds.

**NOTE 10 - SUBSEQUENT EVENTS**

- A. Primary Government - Subsequent to June 30, 1999, bond anticipation notes were redeemed in the amounts of \$11.7 million on July 1, \$67.6 million on August 2, and \$.5 million on October 1. On October 27, bond anticipation notes in the amount of \$68.2 million were issued.
- B. Component Units - THDA remarketed Homeownership Program bonds issue 1998-3C in October for \$40 million. THDA redeemed 1974 and 1985 resolution bonds in July for \$86.562 million and redeemed convertible notes in August for \$27.225 million, and redeemed \$56.275 million of bonds and convertible notes in September. In July and October, THDA issued Homeownership Program bonds, issues 1999-2 and 1999-3, for \$150 million and \$110 million.

On July 16, 1999, the University of Tennessee transferred its sole ownership in UHS Ventures, Inc., a component unit formerly known as University Health System, Inc., to a newly formed 501(c)(3) corporation also named University Health System, Inc. On July 29, 1999, the university transferred ownership and control of its hospital, UT Memorial Research Center and Hospital located in Knoxville, to University Health Systems, Inc., (UHS). The Lease and Transfer Agreement provides a 50-year term for the lease of real property and buildings of the existing hospital and Graduate School of Medicine from the university to UHS.

In conjunction with the University of Tennessee's hospital conversion, the Tennessee State School Board Authority defeased \$96.4 million of commercial paper and \$52.85 million of bonds on July 29, 1999. In November, TSSBA issued \$13.29 million of Qualified Zone Academy Bonds (QZAB's) to finance improvement loans to qualifying K-12

**STATE OF TENNESSEE**  
**NOTES TO THE FINANCIAL STATEMENTS (Continued)**  
**JUNE 30, 1999**

schools in the state. The bonds are part of a federal government program in which a federal tax credit is given to investors in lieu of interest. Also, subsequent to June 30, the authority issued \$19.45 million in commercial paper.